reason
JUNE 1980 $2.00

SPECIAL FINANCIAL ISSUE

HOWARD RUFF
DONALD HOPPE
JAMES DINES
JULIAN SNYDER
J. ANTHONY BOECKH

SURVIVING AN INFLATIONARY WORLD

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"Inflation is confiscating the wealth of America. The next three or four years could bring inflation rates higher than 50%. Right NOW you must literally think differently if you want to survive financially." — Howard J. Ruff, author of HOW TO PROSPER DURING THE COMING BAD YEARS

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— with —

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A MESSAGE FROM HOWARD J. RUFF

How I wish you could have been with the 4,000 who attended our Third Annual Convention in mid-March.

It was a very satisfying experience to bring these friends such a distinguished roster of experts, both as featured speakers and as leaders in our in-depth workshops.

Even though you could not be with us, I'd like you to have the same opportunity to hear these leading authorities and to benefit from their advice.

Through the magic of tape we can do just that. Please read the details on how you can hear every important prediction, be guided by the same advice, know what to expect and how to plan in the year ahead — just as though you'd actually been in San Diego.

I urge you to send in your order without delay, as every day brings fresh economic problems that these experts can help you with.

Best wishes,

Howard

HOWARD J. RUFF

P.S. if you *did* attend the convention, but did *not* order your two-volume set of cassettes, here's another opportunity to own a permanent record of those important convention days.

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- **DR. GARY NORTH,** editor and publisher of "Remnant Review" — Price Controls and What You Can Do to Prepare for Shortages That Will Result"
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— plus —

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HOW TO REDUCE THE DANGER OF A TAX AUDIT

"I'd do almost anything, even *over* pay my taxes, to avoid having the IRS audit my return." A surprising number of taxpayers feel this way.

But this attitude is more usual: "I minimize my taxes as much as I dare — but I also worry about getting slapped with a tax audit."

Then there's a third attitude, more common than you might think: "Those SOBs don't scare me. I'll fight them all the way."

Which attitude resembles your own? Whichever it is, if you earn $25,000 a year... or if you own a house or some other asset that interests the tax collector, there's a new Report you should see:

THE TAXPAYER'S AUDIT SURVIVAL MANUAL

How to Avoid an IRS Audit First and Foremost — And How to Survive One If They Catch You

The authors? You won't find two who know more about this problem. Charles W. Schoeneman, formerly with the U.S. Tax Court, is now a Washington tax attorney (with an imposing client list). Vernon K. Jacobs, nationally known tax consultant and lecturer, is the author of *Taxpayers' Counterattack* and editor of the consumer's tax service, TAX ANGLES (and, therefore, a master at reducing tax gobbledygook to plain English).

Your Chances of Getting Audited

The authors give you the latest figures, broken down by income... the latest reports on tax delinquents, and how many had their property seized. They follow your tax return, step by step, throught the IRS bureaucracy. This "tour" gives you precious hints on how to lessen your chance of an audit. For example:

- How to choose a tax advisor. (Careful: the one you pick might *cause* you to be examined.)
- Fearsome weapons the feds can use: liens, levies, seizures. What each one means. How they hurt you in *other* ways.
- One powerful weapon to get the IRS to cut your tax deficiency. (Here, the odds are in *your* favor.)
- What to do if a tax agent shows up at your door unannounced.
- How to make the tax man suspicious: more than 25 signals that suggest tax fraud. Signals given off by the tax man that hint at a criminal investigation.
- When the exam period ends, collection begins. Do you have any recourse then?

Valuable Extras

- Official IRS List of Unallowable Deductions
- IRS Guidelines for Auditing Professionals
- 20 charts, illustrations, IRS forms
- Map of IRS districts

- Encouraging note: the double screening your return must pass before you get audited.
- Should you round off your figures?
- The awesome legal powers of Special Agents and Revenue Agents. How they differ.
- Can your accountant be required to testify against you? How about your wife? Your children? Can your accountant be forced to produce your tax records?
- Useful literature you can get free from the U.S. Tax Court.
- True or false: when a taxpayer beats a criminal rap, he may still owe a big tax bill.
- Should you go before the IRS yourself, or send your tax advisor? 3 possibilities.
- One reason not to file an amended return.
- Your chances when you appeal (better than you think).
- Form 870: does it ever pay to sign it on the spot?
- When the IRS suspects fraud: what goes on behind the scenes.
- Should you ever admit a mistake? A doubtful deduction?
- What are the mathematical chances of being prosecuted for a tax crime? Of being convicted? Of going to jail?
- Priceless advice on how to conduct yourself during the audit. Tips that help it run *your* way. Dangers to avoid.
- Why the odds against you aren't so bad after all.
- When is the best time to file — early, late, or just under the wire?

One thing that make an IRS audit so unsettling: much of it operates outside the American legal system. The tax bureaucrats assess what they will. The taxpayer must *prove* his deductions: guilty till proven innocent. It *is* an adversary situation — and the tax collector holds all the guns. So if you pay a sizable tax bill, you owe it to yourself to see how far you can legally minimize your taxes — and what risks you may be taking at each step.

The stakes are high. In 1978, the average *extra* assessment gathered in by the IRS came to $3,898. It is almost certain to soar over $4,000 for 1979 returns — and keep soaring. This new *Manual* comes just in time.

FREE EXAMINATION

The *Manual,* frankly, is prepared for those who make $25,000 or more... who can save the most... who have the most to lose. It is tax-deductible and comes as a typewritten Special Report for $35 postpaid, and is returnable for a *full* refund within 30 days.

Nothing can *guarantee* you won't be audited. Sometimes it's just bad luck. But if you don't agree that the *Manual* cuts your chances of an audit, just send it back to Alexandria House Books, 901 N. Washington Street, Alexandria, VA 22314. You'll get your $35 back, and no questions asked.

How to get this Special Report FREE

You may take this $35 Report FREE with a two-year subscription to TAX ANGLES, the only monthly service that shows executives, owners of small businesses, professionals and investors how to cut their taxes *legally.* Just check the box in the coupon and send $79 for 24 issues (two years). GUARANTEE: Read 4 issues. If TAX ANGLES isn't worth many times its modest price in tax savings, just tell us to cancel after 4 issues. We'll send you a complete refund for the entire unused portion of your subscription — and you keep the *Manual* FREE.

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June 1980/Vol. 12, No. 2

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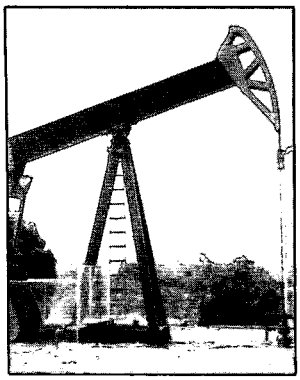

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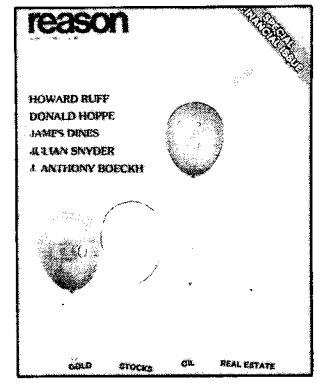

Cover photo by Kelley Dwyer

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ISSN 0048-6906

Alex Laurins, Attorney, and International Financier can tell you how to

MAKE MORE MONEY . . . . . AND KEEP IT

Using Offshore Banking and Trusts.

Dear Friend,

Every year, every month, your money buys less. When you do make a profit, the government grabs the lions share. Rampant inflation exists side-by-side with recession. Governments who can't control their own bureaucracy try to monitor and control every facit of their individual citizens' lives. You worry about how to provide for your family, today and tomorrow.

What is the answer? How can we control our lives and our assets? I believe the best solution is to adopt an international financial approach, with confidential transactions, diversification into hard assets and currencies and avoidence of taxes wherever possible. You don't have to be a Rockefeller to do this. Even a person of moderate means can reap the benefits enjoyed by wealthy individuals and multinational corporations. It is simple once you know their secrets.

I learned these techniques the hard way. I have set up an offshore bank and have prospered in spite of U.S. government bureaucrats. My associates and I believe that you should know the alternatives available that can enable you to control your financial life. There is some literature available on the philosophy of privacy, internationalism and hard assets, but we found very little explaining actual techniques and examples. We wrote **How to Profit from Offshore Banking** and **Anyone can Profit With a Secret Foreign Trust** to fill that gap with information not available anywhere else—case histories, forms, contracts, and step-by-step instructions.

You owe it to yourself and your family to read these books. If you use the ideas presented you *will* protect and increase your assets. If you don't use them you will have, at least, made a decision based on knowledge of all the alternatives.

We guarantee that you will find value in **How to Profit from Offshore Banking** and **Anyone Can Profit With a Secret Foreign Trust.** If you don't, just send the book back for a full refund. We don't think you will want to.

Yours faithfully,

Alex Laurins

LEARN THE SECRETS MILLIONAIRES AND MULTINATIONAL CORPORATIONS HAVE KNOWN FOR YEARS

HOW TO PROFIT FROM OFFSHORE BANKING explains how to:

- *use bank secrecy*
- *start your own bank*
- *increase your net worth*
- *increase your working capital*
- *protect your assets*
- *write insurance*
- *make loans with no risk*

ANYONE CAN PROFIT WITH A SECRET FOREIGN TRUST tells how to:

- *move money secretly*
- *confidentially correspond with your trustee*
- *control and transfer the assets of your trust*
- *plan your estate*
- *use trusts to avoid income taxes*

By the time you finish this book you will know whether you need a trust, how to set one up and how to use it.

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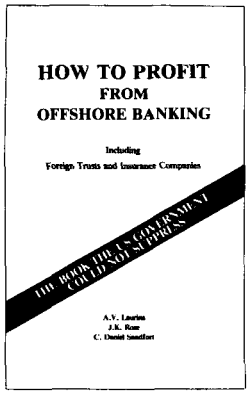

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☐ Send me ____ copies of **HOW TO PROFIT FROM OFFSHORE BANKING** at $20.

☐ Send me ____ copies of **ANYONE CAN PROFIT WITH A SECRET OFFSHORE TRUST** at $10.

☐ I want *both* books for the reduced price of $25. Send me ____ sets.

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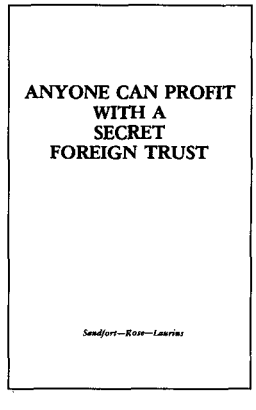

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The IRS Can Seize Your Property Whenever It Wishes

Yes, that frightening headline above is absolutely true.

Under a "jeopardy assessment," the IRS may confiscate a taxpayer's property whenever it deems necessary. It may seize your house, your car, your stocks, your bank account. To do all this, it needs no court—just its own suspicions.

But that's just the beginning! All cash transactions over $10,000 are automatically reported to the Treasury Department. Banks routinely photo-copy all your correspondence, deposit slips, and the fronts and backs of all your checks. Your tax return requires you to list all your foreign bank accounts. And a mistaken credit report can destroy you financially.

The financial snoopers—and how they can hurt you.

Every single day, in countless ways, your financial privacy is invaded and destroyed.

The consequences can be severe: The loss of your freedom to travel, to invest, to keep the money you've earned. Gossip and threats to your reputation. Divorce and malpractice lawsuits. The risk of theft. A tax audit. And if you're just a bit different from everyone else in your political views or religious beliefs, the possibility of becoming a target of government surveillance.

Now for the good news:

You can regain your financial privacy.

Fortunately, it *is* possible to keep your financial affairs safely out of the prying eyes and hands of the professional snoops. One book—and only one—will show you how: **Mark Skousen's Complete Guide to Financial Privacy.**

Skousen has a Ph.D in banking and monetary economics from George Washington University and is the author of several best-selling books on investment and financial topics.

This brand-new book is based on more than a year of investigative research by Dr. Skousen—which he spent plowing through government documents and consulting with experts in every field.

What you'll find in Mark Skousen's Complete Guide to Financial Privacy.

Here's a small sampling of the wealth of helpful, practical information and advice in this book:

- What have you got to hide? An eye-opening look at how much they know about you—and what you stand to lose as a result.
- Ten smart techniques for keeping your banking affairs confidential.
- The facts about Swiss banking secrecy.
- The Swiss "numbered account"—is it for you?
- Keeping your correspondence and phone conversations private.
- Tax havens and foreign trusts: how to use them for privacy and profit.
- How to beat the foreign financial reporting requirements—five perfectly *legal* techniques!
- Nine ways to send money abroad undetected—and six ways to bring it back.
- How to move gold, silver, coins and diamonds out of (and back into) the United States.
- Just how private *is* an unlisted phone number?
- Which of your investments are reported to government agencies? (And eight which are *not!*)
- Obtaining loans without revealing their purpose—even to your banker!
- Your credit file—how to find out what everyone else knows about you.
- Hiding your valuables: safe-deposit boxes, private vaults, secret caches.
- How private are your dealings with employees and professional advisors? Your secretary? Accountant? Investment specialist? Attorney?
- Privacy and your will: avoiding the expense, delay and publicity of probating your estate.
- Privacy Directory: sources of information and advice you can use.

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Mark Skousen's Complete Guide to Financial Privacy will show you how to become a financially private person once again. This remarkable book is 233 pages, hardbound, indexed, and packed cover-to-cover with useful, readable information and advice. The price is just $14.95 postpaid— a small sum when your financial privacy and freedom are at stake.

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editor's notes

• **FAA FOLLOW-UP.** Our January 1979 issue lambasted the Federal Aviation Administration for doing a poor job of operating the nation's air traffic control system and mentioned the San Diego airport area as a particularly bad example. In March of this year the FAA at long last announced that it will be upgrading the air safety procedures in San Diego by putting in a Group II Terminal Control Area as of May 15. San Diego will be the 24th city to have a TCA—a system of procedures and equipment aimed at providing more positive control of air traffic in congested areas.

One of our article's main points was that the FAA tends to await major disasters before taking significant steps to increase safety. That assessment has been confirmed by the General Accounting Office in a major study of the FAA's handling of 16 safety areas. In a summary of its 105-page report, GAO says, "FAA does not have effective systems for identifying safety hazards, a comprehensive planning process to address safety issues, an adequate system for planning and approving individual safety programs, a proper system of controls to govern the implementation phase of safety projects, or sufficient evaluation of safety programs and projects." Rep. Elliott Levitas (D-Ga.) called the GAO study "a damning indictment of the management of FAA's primary responsibility—the lives of the traveling public."

• **SPECIAL OFFER.** Readers of this Financial Issue will note that the debate on inflation versus deflation, beginning on p. 28, took place at the sixth annual conference of the National Committee for Monetary Reform. A complete set of cassette tapes of this four-day affair, totaling 24 hours of lectures, seminars, and question/answer sessions with 40 speakers, is available from NCMR. The normal price is $140, but REASON readers may order the complete set for just $75—46 percent off. Write NCMR, Dept. R, 8422 Oak Street, New Orleans, LA 70118.

• **ADDRESS, PLEASE.** Several readers have asked us for the address of Antony Fisher's new Pacific Institute (Feb., p. 42). You can contact the Institute at 220 Montgomery Street, San Francisco, CA 94104, phone (415) 788-1966.

• **SUMMER SEMINAR.** The Reason Foundation/Liberty Fund summer research seminar in legal and moral philosophy will get under way in mid-June. Thirteen young scholars have been selected to participate in the 12-week seminar at the Foundation's offices in Santa Barbara. Each will pursue his own research within the general subject area of legal/moral philosophy and will take part in seminars with visiting scholars. Last year's similar program enabled several of the research fellows to complete books and led to a number of articles being submitted to scholarly journals.

• **DEFENSE INTEREST.** Cong. Ron Paul's article "SALT-Free Defense," published in our March issue, has been reprinted by the US Air Force's *Current News* (Mar. 18, 1980), a publication read by key Department of Defense personnel and members of Congress.

• **UFW UPDATE.** The latest journalist to question the actions of Cesar Chavez and the United Farm Workers union is none other than columnist Jack Anderson. Documenting cases of violence and conflict of interest in UFW operations, Anderson concludes that the UFW "has become a violence-prone, tyrannical empire under the iron-fisted rule of Cesar Chavez." Echoing charges in REASON's path-breaking article on the subject (Nov.), Anderson says "Chavez seems to have lost sight of the people whose welfare earned that [earlier] respectability."

One of the important issues raised in REASON's article was the UFW's Citizenship Participation Day fund, to which UFW workers are required to contribute. Under California law, the UFW was allowed to define "good standing" in the union to exclude any member who refused to allow his or her "contribution" to be placed in the union's political action fund (used to back friendly politicians). Workers not in good standing could be expelled from the union—and therefore from their jobs. The California legislature is close to passing a bill to restrict the "good standing" definition to refer only to payment of union dues—as is the case under federal labor law. With Gov. Jerry Brown ready to veto the bill (as he did a similar one in 1979), the state Agricultural Labor Relations Board on March 20 attempted to preempt the issue by ruling that UFW members can no longer be compelled to contribute to the fund. They will now be able to request a refund from the union in writing. At press time, the bill had passed the Assembly and was awaiting action in the Senate.

—R. P.

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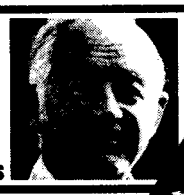

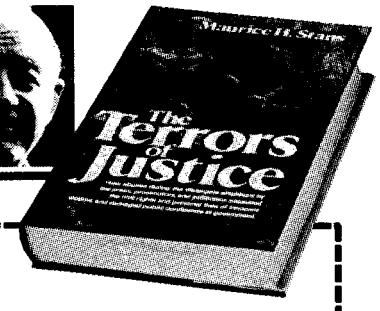

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Protecting Whom?

editorial

First he threatened the federal government with bankruptcy and the implied costs of unemployment and monopoly in the auto industry. A cowed Congress granted his firm $1.5 billion in loan guarantees. But that wasn't enough for Chrysler chairman Lee Iacocca. On top of federal subsidy, he now wants the government to force consumers not to buy some of his competitors' products.

Yes, you read that correctly. In an interview with the *Wall Street Journal* on March 11, Iacocca said that he favors federal legislation to slash imports of cars from their current 30 percent market share to the 17 or 18 percent they held in 1978. In other words, about 42 percent of those who wanted to buy a Japanese or German car would be forbidden to do so—and those who *could* do so would end up paying a premium price for it.

Iacocca's is not the only voice urging such anticonsumer measures. Cong. Charles Vanik several days before had warned Japanese automakers to cut back their exports to this country to 1977 levels "or face more drastic action through legislated quotas." Meantime, United Auto Workers president Douglas Fraser went to Japan to threaten the carmakers with retaliation if they didn't open plants in this country. On his return (after receiving no such commitments) he began urging legislation to require "up to 75 percent North American content" in imported cars. Perhaps the ultimate extension of this philosophy is a current proposal by Britain's largest union to ban all auto imports by 1982, in order to "protect" dying British Leyland.

What a morally despicable thing is "protectionism." What right has government to interfere with the liberty of consumers to purchase whatever automobile they may prefer—or with the liberty of producers to sell whatever cars they can to willing buyers? There can be no moral justification for using force to prevent such transactions.

Millions of American consumers have made it clear by their purchases that they prefer compact, well-made, fuel-efficient Japanese and German cars. Surveys of 10,000 American households in 1978-79 by the Motor & Equipment Manufacturers Association revealed that imports strongly outrank US small cars in perceived fuel economy, engineering, and durability. A recent survey by *Ward's Automotive Reports* found that almost half of *Detroit's own engineers* think that Japanese cars rank highest in quality; American cars placed a distant second (at 27 percent). Even Lee Iacocca concedes that "the Japanese have earned their reputation for quality."

But protectionism does more than just violate the rights of the consumers and producers directly involved. It harms countless others, as well. One very visible group of victims is the Americans who work for imported-auto dealers. As Joseph Coberly—himself a Ford dealer—pointed out recently in testimony before Congress, there are 4,500 foreign car dealers, employing some 140,000 people. "By what standard should they be sacrificed to the 150,000 UAW members now on indefinite layoff?" he asked. Coberly also pointed out how another protectionist policy—restrictions on low-priced steel imports—increases costs to American automakers by $50 to $75 a ton. Protectionism is not only immoral; it flies in the face of sound economics.

US automakers would also suffer from Douglas Fraser's proposed local-content requirement. If the US government imposes such a rule, other governments will follow suit. And *that* will torpedo the plans of Ford and GM, among others, to produce "world cars"—utility vehicles assembled from components produced wherever it is most economical to do so.

The concept of a world car illustrates a basic principle of free trade: the international division of labor. By allowing resources to be utilized wherever it makes the most economic sense—doing labor-intensive operations where labor is cheap, electricity-dependent operations where electric power is cheap, etc.—the total amount of goods and services that can be produced is maximized. Interference with this process, whether by subsidizing infant industries or shielding them with tariffs, or by restricting imports and exports, is inherently wasteful and is literally counterproductive.

The principle of comparative advantage is so powerful that it even makes sense for a country to go it alone, eliminating its own tariffs and quotas even if other countries keep theirs. As evidence, witness the success of tariff abolition in 19th-century England, post-World War II Hong Kong, and today's Chile. In the latter country, the rapid, unilateral slashing of tariffs has led to a major restructuring and revitalization of the economy.

But the most important practical argument against auto protectionism is that it could well set off a new trade war among nations. For the past several years pressures in that direction have been building up. Reports Britain's National Institute for Economic and Social Research, the fraction of international trade in manufactured goods under government control went from 13 percent in 1974 to 21 percent this year—up 62 percent in just six years.

The last great period of trade war was the 1930s. The Smoot-Hawley Tariff imposed major increases on thousands of imported products, thereby turning a business cycle contraction into the Great Depression, not just in this country but around the world. Today American industries like steel, footwear, and even semiconductors are calling for increased tariffs or quotas on imports. The same thing is occurring all over Europe. The *Wall Street Journal*'s Philip Revzin notes ominously that "some trade experts fear that a few more protectionist acts in sensitive industries such as chemicals and autos could touch off a major international trade war, sending everyone scurrying behind tariff and quota walls." And, unfortunately, once such a trade war begins, it is the developing countries that are generally hurt the worst.

Think about that when you go to buy your new Datsun 280ZX. The Lee Iacoccas and Douglas Frasers who seek to forbid you from doing so are not simply interfering with your freedom of choice; they are endangering the economic well-being of countless millions of people around the world.

Robert Poole, Jr.

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Dr. Franz Pick is one of the world's most respected authorities on currency matters and precious metals. He studied currency and inflation theories at the University of Hamburg and the Sorbonne in Paris. His degrees include BS, MA, MBA, LLD, and PHD. He is the Publisher of *Pick's World Currency Report* and *Pick's Currency Yearbook*, two internationally respected publications on currencies. He is the author of 6 books on silver and gold.

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On Traditional Investments

"Currency debasement destroys the value of corporate bonds, stocks, life insurance policies, annuities, and all other debt instruments denominated in dollars. We may be the richest nation in the world, but our assets are melting away before our eyes and virtually no one recognizes this fact."

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letters

Gofman Objects

I wish with all my heart that I could believe Bernard Cohen ["Radiation Fantasies," Mar. 1980]. I wish I could believe that nuclear power will be safe, for I do not enjoy spending one moment of my life span on this dreary subject. However, I am unwilling to cripple my brain with wishful thinking, and I cannot ignore the evidence which shows Cohen is wrong both about the toxicity of ionizing radiation and about the containment of the radioactive poisons.

It would take a "letter" just as long as Cohen's article to correct the errors and distortions in virtually every paragraph of what he wrote, and to make it possible for REASON's readers to understand *why* experts disagree. Since I was not offered the space, REASON's readers will have to go elsewhere to understand this issue.

If REASON had had any intention of helping its readers arrive at the truth, it would not have invited only a leading nuclear power advocate to present his views. By doing so, REASON's editors showed contempt for their readers....

Now, here's a fair question: Why didn't Gofman protest when *Libertarian Review* presented only one side of the issue? The answer is that it is impossible for someone who respects the truth as I do, to insist that untruths be published. If nuclear advocates would stick to opinions and stop adorning them with scientific falsehoods, I would be an advocate of presenting "both sides...."

In allegedly libertarian magazines, it is particularly astonishing to see the editors resorting to arguments from authority ("consensus of expert opinion," etc.), when all libertarians have to ignore the overwhelming consensus of expert opinion about economic truth in order to be libertarians!

And all scientists know that every new scientific insight starts with the insight of a tiny minority—usually a single individual. How fast a new insight gets confirmation by the work of other scientists varies from a few years to a century or so; acceptance takes even longer than confirmation, of course. My work is doing very well with respect to confirmation by additional evidence, and rather poorly with respect to acceptance. The latter is not surprising, since the part of the scientific community concerned with radiation exposure has a great deal to lose by the acceptance of my work.

One very important argument for libertarianism is that many humans are too corruptible, nasty, and unscrupulous to be entrusted with power over other humans. Scientists are certainly no exception when it comes to corruptibility, and intellectual honesty is very commonly sacrificed for grants and personal advancement.

It is the joke of the decade for REASON to present the BEIR, ICRP, NCRP, and UNSCEAR radiation committees to its readers as if these committees were something other than collectives riddled with conflicts of interest. Thoughtful readers will ask themselves, "When both motive and opportunity exist, will intellectual crimes be far behind?" Scientific evidence has thoroughly discredited much of the nonsense about radiation hazards put out by BEIR, ICRP, NCRP, and UNSCEAR committees. I have no doubt that further scientific *data* will decimate the remaining nonsense issued by such committees....

John W. Gofman
San Francisco, CA

The editors reply: We have not asked Dr. Cohen to reply to the above letter because of its tone and its lack of content concerning nuclear radiation. But inasmuch as Dr. Gofman's target, anyway, is REASON, we thought we should answer his letter.

Dr. Gofman wasn't offered the space for several reasons. For one, he's had space already in other publications likely to be seen by our readers, publications that did not bother to feature anyone who disagrees with him. For another, REASON sticks by its name, and we have not seen Dr. Gofman produce any sort of calm, measured discussion of the facts and issues involved. We would not have accepted for publication an article that presented Dr. Cohen's analysis, either, if it were peppered with vitriolic accusations, argument by inference of suspicious motives, anecdotal recounting of uncheckable private conversations, and so on. Much of Gofman's letter has nothing at all to do with nuclear energy and the morality of producing it. If this is what he has to offer our readers, why should anyone think of him as a prime candidate for inclusion in a careful, civil discussion of an important issue?

To the claim that Dr. Gofman did not demand that publications where he has appeared also open their pages to other views of the matter, because "it is impossible for someone who respects the truth as I do, to insist that untruths be published," we might say, "Ditto." But we realize that in some cases—and maybe in this one concerning nuclear energy production—the

truth is yet to be fully identified, so having different positions presented may be extremely useful to citizens who, because of the unfortunate politicization of energy production, are required to make a judgment concerning scientific matters. And while not only libertarians but the general public have plenty of occasion to read the views of those on Dr. Gofman's side of the issue, they are rarely offered the other side, let alone a nontechnical explanation of the facts and terms of the debate.

Perhaps the only apparent substance in Gofman's letter is his calling into question what he calls "arguments from authority ('consensus of expert opinion,' etc.)." REASON did not leave the matter at such consensus but explained how the various scientific committees were formed and who is involved in this consensus. This enabled our readers to go way beyond "argument from authority" in assessing the merits of Cohen's case. Moreover, for Gofman to invoke a view of scientific change and imply that, because his view is accepted by a minority at this time, it must be right, is simply the other side of the coin of the irresponsible reliance on authority of which he accuses REASON.

It is not necessary to go further. Dr. Gofman is great, we admit, at impugning people's motives, as his letter demonstrates. We trust our readers will not succumb to this tactic.

Well Done

Congratulations on the March 1980 issue of REASON. The Bernard L. Cohen ("Radiation Fantasies") piece ought to be required reading for legislators everywhere at every level. It's the most down-to-earth, factual exposition of the true risks to the population from our nuclear programs that I've seen.

And the tritium piece by Marshall Brucer—what can one say? How utterly ridiculous and stupid can people be—including the supposedly unbiased press?

When will REASON undertake to survey and give us a factual report on the subject of nuclear waste disposal?

Robert W. Poole, Sr.
Fort Valley, GA

The editors reply: Nuclear waste disposal will be the subject of an upcoming cover story.

Free Market Power

I was impressed with your article in the March issue debunking the antinuclear forces who appear to be gaining influence in the libertarian movement. I'm anti-government-supported nuclear power just as I'm anti-government-supported coal or

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petroleum power generation, but this isn't the way the antinuclear case is often presented by self-proclaimed libertarian publications. Sure, libertarians can join with conventional antinuclear nuts in using absurd propaganda about the effects of radiation to get antinuclear votes. But is it acting on principle to use lies to manipulate the public into voting the right way (i.e., anti-government-supported nuclear power) for the wrong reason? I think not.

So, here is my three-year renewal. Please continue your advocacy of radical libertarianism in which the free market is free to choose the best type of power-generation as well as the best everything else.

Jim Cartwright
Austin, TX

Radiation Politics

Last year, I and a number of other writers whose articles appeared in the July/August issue of *Libertarian Review* were severely criticized by a group which included the editors of REASON for "taking a political stand on a technological issue" and "opposing nuclear power *per se*." Yet it seems that REASON has committed the same sin with its March 1980 issue.

"Radiation Fantasies" by Bernard Cohen rather blatantly *endorses* nuclear power "*per se*." Rather than politicizing the issue where it shouldn't be, however, Cohen totally ignores the very real and important political implications of the technological issue he discusses.

Nowhere, for instance, does Cohen mention that the people who are seeking government licenses to operate nuclear plants on the basis of safety assurances such as he offers are operators of public utility monopolies, not honest entrepreneurs seeking merely to be allowed to compete in the marketplace for energy consumers' dollars. Neither does he mention the Price-Anderson Act, passed after the relentless testimony of nuclear industry representatives that potential investors in their plants would not take the risks which Cohen asks the public to take.

A glaring absurdity is Cohen's appeal to authority about the dangers of radiation. Every one of the committees which Cohen quotes as certifying the relative harmlessness of radiation is a government-run and -funded agency. Most are creatures of governments actively involved in nuclear weapons and nuclear power development. Does Cohen—or REASON—seriously expect us to trust such people to tell us what is and is not good for us?...

The Cohen article clearly endorses a go-ahead for the existing nuclear power industry in this country—a cartelized industry fueled mostly with tax dollars and conceived and maintained under shrouds of government secrecy. This secrecy not only prevents private ownership of nuclear materials (something else which Cohen neglects to mention), but also keeps reliable, checkable information about those materials and the hazards associated with them from reaching the public. The growth of this industry will, further, imperil the privacy and other civil liberties of an ever-growing number of Americans, a hazard which, politically, is far more significant than any physical hazard from radiation but which, like the Price-Anderson Act, is always ignored by those promoting nuclear power on the basis of its alleged safety....

Patrick L. Lilly
Colorado Springs, CO

The editors reply: Dr. Cohen's article was an attempt to explain in nontechnical language the extent of the risks associated with nuclear power generation, risks with which much of the public is quite concerned. Since Dr. Cohen is a nuclear scientist, and not a political theorist or pundit, to have asked him to amend the article he submitted for publication, to include consideration of political matters, would have been irresponsible on our part. We have, of course, published discussions of the political issues involved, including Sheldon Richman's repudiation of Price Anderson in our November 1979 issue.

Fear Fossil, Too

A friend passed on to me a copy of your recent feature on radiation fantasies by Dr. Bernard Cohen. I must commend you and the staff of REASON for your attention on this important subject.

Nuclear power is not 100 percent safe, but it is much safer than any other energy production system that exists. If John Gofman has such an incredible fear of radiation, I suggest that he try to also close all fossil fuel-fired power plants, since they discharge more radiation (as well as hydrocarbons) than the entire nuclear fuel cycle. Gofman would then be in an excellent position to lead all Americans on a quest to follow Iranians into the 7th century.

Having been impressed with your editorial stance on many other issues, also, it's about time to start a subscription. Please send me the appropriate form.

Jack Challem
Santa Fe, NM

Review Full of Holes?

John Hospers's review of *Star Trek* and *Black Hole* were fairly accurate. However, he misses the point of science fiction when he criticizes *Black Hole* for not conforming to current scientific dogma.

Faster-than-light travel, time travel, direct transmission of matter, etc., are old hat to sf readers and all impossible by es-

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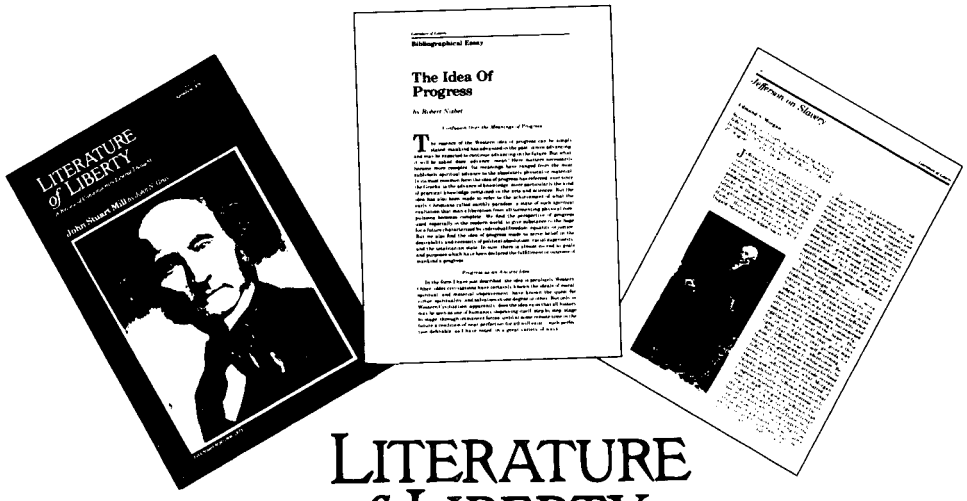

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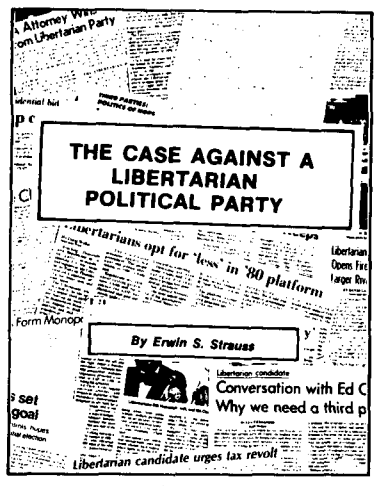
THE CASE AGAINST A LIBERTARIAN POLITICAL PARTY
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Conversation with Ed C
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tablishmentarian views of reality. I would not be the first to point out that space travel and atomic power were likewise "impossible" two generations ago, when Hospers was young. Also, there are reasons to believe that it is possible to ride down a black hole and emerge somewhere else from a white hole (a "cosmic gusher"); see, for instance *The Iron Sun* by Adrian Berry. As far as the ability of the Disney studios to outpace current technology goes, one need only consider that in 1953 it was they who commissioned Wernher von Braun to be science advisor for their movie *Man in Space.*

Finally, it is interesting to note that the concept of a black hole was originated by Immanuel Kant in 1750. He posited it as a reductio ad absurdum to Newtonian mechanics; his analytic-synthetic dicotomy would not allow a body so massive that even light could not escape its pull. Please let it be noted that in 1980, John Hospers stated that traveling through a black hole is impossible.

Michael Marotta
Lansing, MI

Tax Information Helps

Your January tax tip on investment dividends [Taxes] allowed me to deduct $271 as a tax credit, which as you know means that I could reduce by that amount the tax determined from computations from the tax tables. My congratulations on allowing us that tidbit of tax saving!

Charles J. Eggerstedt
San Luis Obispo, CA

Point Taken

In the February 1979 issue of REASON I had an article on Sweden. The main topic of the article was government interference in private life, and continued socialism, in spite of a nonsocialist government. I also criticized an overambitious bureaucracy.

This very bureaucracy found its opportunity for revenge when REASON sent me a number of extra copies of the issue. These were free extra copies, given to the author of an article free of charge. Nevertheless, the customs authorities found that I had to pay value-added tax as well as an administrative fee for customs clearance. This was completely against the rules, which allow minor gifts to be imported without paying value-added tax or fees. I thus refused to pay the fee and asked the post office to return the magazines to the customs office, in order to get them classified as goods free of value-added tax. When the customs official refused to change his mind, I appealed to the Royal Customs Board ("Royal" in Swedish administrative practice meaning national, as opposed to local). At the same time I asked the post office to keep the magazines in the country

(Continued on p. 69.)

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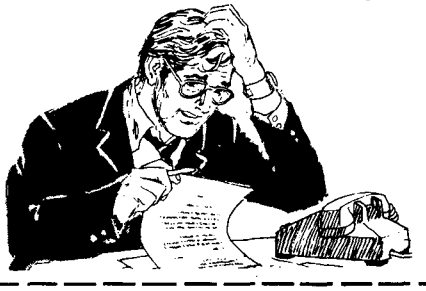

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Economic Research Bureau Warns:

When the Depression Hits, What Happens to You?

(Washington, D.C.) A major economic crisis is about to hit the United States, and our government is not going to be able to head it off. This is the controversial opinion of Dr. Gary North, the executive director of the American Bureau of Economic Research, the nationally known research organization. In fact, Dr. North argues, the government's own policies are the source of the coming collapse.

"The U. S. economy is a house of cards," Dr. North asserts, "but people who didn't go through the Great Depression can't believe that such a thing is possible any more. We have raised up a generation of Americans who simply won't know what to do when the crisis hits. Their grandparents remember what real hardship is, but the kids don't want to think about it."

"The Six Deadly Assumptions"

Millions of Americans, young and old, are making assumptions about the future that are dangerously optimistic. Dr. North calls these "the six deadly assumptions." A lot of people believe in all six, he says, and practically everyone believes in at least four. The six assumptions are these:

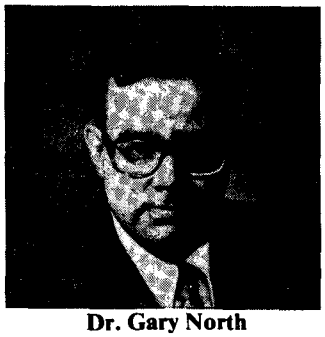
1. **"My pension can actually be paid off."**
2. **"The Social Security system isn't bankrupt."**
3. **"The Federal government insures the present and future value of my bank account."**
4. **"A depression is impossible today."**
5. **"My guaranteed annuity is safe."**
6. **"The government will control inflation."**

If you have made even **one** of these assumptions, and you refuse to rethink your premises, Dr. North warns, "you are headed straight for disaster."

"Special Report"

Dr. North's detailed predictions about the immediate economic future, plus his analysis of the six deadly assumptions and how to escape their consequences, are now available in a special report, ***How You Can Profit from the Coming Price Controls.***

The government will soon be issuing a new currency, he says: ration coupons. He also predicts crippling shortages. Whole sections of the economy will go bankrupt. Unemployment in these industries will skyrocket. Businessmen who have not learned the techniques of capital preservation under price controls will have a terrible time. "As always, sharp traders who know in advance what is coming will clean up," he predicts.



Dr. Gary North

Will the Government Suppress his Report?

Dr. North claims that his special report gives you the techniques that will "beat the paralyzed markets." He says you have to know about timing, shifting markets, hidden sources of supplies, and barter. "These techniques are really not that hard to master once you know what they are, but they aren't obvious to most people. You have to be taught."

Dr. North admits that very few people will take the steps necessary to protect themselves. "This is why the little guy always gets sheared. People refuse to act until it is way too late. They won't read a survival manual like ***How You Can Profit from the Coming Price Controls.*** But for those who do, and who follow its advice, the coming crisis should be a time of tremendous opportunity. For some people, it will be a true bonanza."

"The Government Will Suppress This Report"

Dr. North is pessimistic about the long-run prospects for his report. He is convinced that the government will eventually take steps to restrict its circulation. "My report shows people how to beat the controls. The bureaucrats resent this. After all, what good are the controls, from the government's point of view, if people know how to short-circuit them? That's what my report is all about."

About the time that most people finally figure out that a crisis has hit and that they desperately need the information in his report, Dr. North says, the government will force it off the market. "People always think they can get special information anytime they need it, but they can't. If they wait too long, they will have to pay through the nose to get it."

There are still some important **loopholes** that the government has neglected to close, Dr. North insists, but they won't be available forever. "That's why the people who act now will make the big money. Those who wait around will **pay** the big money." If you hesitate now, concludes Dr. North, "you're asking for trouble."

Dr. North's special report, ***How You Can Profit from the Coming Price Controls***, is being distributed by the American Bureau of Economic Research. It sells for $14.50. To order, fill out the coupon below.

GUARANTEE: If the government should prohibit further sales of Dr. North's report while your check is in the mail, the American Bureau of Economic Research will return your check by first class mail within one working day of its arrival. The Bureau cannot guarantee to send you the actual report if the government acts before you do. **Immediate action on your part is strongly recommended to insure that you receive Dr. North's report.**

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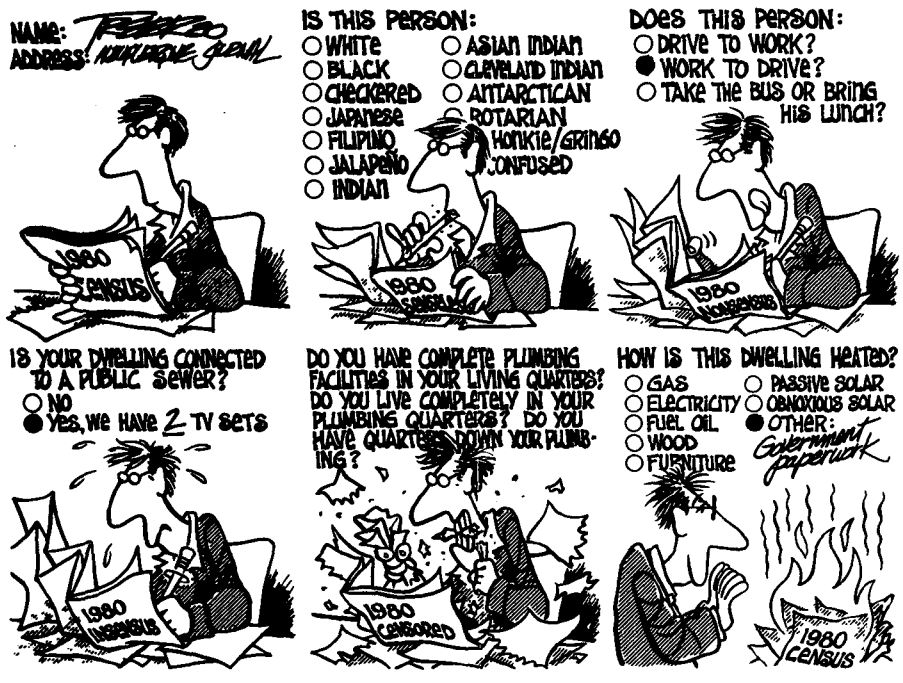
brickbats

☐ **Only a real patriot** can truly feel the monumental advance this nation of immigrants has made, inch by inch. And now, our understanding of the wonders of the universe, and supply and demand, slowly makes headway. From the *Los Angeles Times* lead story of March 16, 1980: "DRIVERS CUTTING GAS USE AS PRICES RISE: Evidence Shows Cost Is More Important in Reducing Consumption Than Believed." (A Nobel Prize is surely on its way.) "The long-held belief that American motorists would pay any price to drive is fast proving a myth. In 1974, after the Arab oil embargo and the quadrupling of world oil prices, many in the United States doubted that increasing prices at the pump would do much to curb consumption. People would give up almost anything, so the argument went, rather than reduce their driving. But six years later, those doubts are being dispelled. Americans have cut back their use of gasoline sharply below what analysts were projecting in the mid-1970s. Moreover, total gasoline use declined 5% last year and continues to drop in 1980, leading most experts to conclude that 1978 gasoline consumption—113.8 billion gallons, or about 16.4 gallons per week for each gasoline-fueled vehicle—will never be matched in the United States. . . . The popular notion that, come hell or high water, Americans would not give up the Sunday drive made it difficult to believe that high prices could help control consumption. But the recent drop in gasoline consumption—nearly 10% in the first six weeks of 1980 contrasted with the same period a year ago—has made more and more analysts and policy makers believe that motorists are not so resistant to change as some had supported." Ahhh. Garbage. (Sounds too much like "economics.")

☐ **The administration** in Washington may be a little loose with the taxpayer's dollar in doling out $2,670 to construct a solar-heated doghouse (the feds want to record the dog's behavior under solar conditions, check its grooming, habits and see what television shows it prefers) and in thrusting another $1,200 into the hands of an eager recipient in Lupus, Missouri, to erect a solar outhouse. Yet Jimmy can, with accuracy, present himself to the nation as an economy candidate this year. The House Appropriations Subcommittee estimates that the "taxpayers will save $3 million in transition costs this year if there is no change in government."

☐ **A setback for socialized medicine** in India: New Delhi surgeons have removed the wrong eye from a girl scheduled for a cancer operation. Now her other one must go as well. (At least they weren't making a *profit* on her, now.) And in a kind gesture that epitomizes the care the welfare state takes when cuddling its minions, the Internal Revenue Service has kindly extended the filing deadlines for the immediate families of those US citizens taken hostage in Iran. See the advantages in overseas travel?



☐ **Yep. He's done it again.** Jimmy Carter has promised to whip inflation with more than a WIN button: to *reduce* the cost of living, the government is *raising* the price of gasoline an estimated 10 cents per gallon. Mel Brooks was not available for comment, but it was rumored in the Capitol that the Hollywood producer-director was upset that the administration had gotten screen rights to the "anti-inflation" farce first. As for the rest that the Prez dished out to a nation up to its ears in double-digits, the *Los Angeles Herald-Examiner* summed it all up right in the following day's headline; "CARTER: 'PAIN,' 'DISCIPLINE.' " And now an entire superpower in bondage.

☐ **Senator Lawton Chiles** (Drunk-Fla.), demonstrating just that certain deftness with the English tongue while pushing the outer limits of human credulity, commenting on President Carter's *first* absolutely lean, austere, minimum federal government expense account (that is, the fiscal 1981 budget): "I applaud proposed increases for Social Security and various health and social services, but the $16 billion deficit projected by the $615.8 billion budget will not help control inflation." It is hard to imagine how a fellow with the talents of the Honorable Mr. Chiles might ever be defeated.

☐ **When the American electorate** was first asked to jump into the Social Security program by Franklin the Great, many considered the idea of helping the country's elderly just splendid. They generally like the notion even better today, owing to the fact that the young adults of the Depression are the senior citizens of today. But now the Urban Institute has crammed some big numbers into an automated computer machine and come up with. . . even bigger numbers: "The elderly's share of the [federal] budget could soar over the next 40 years from about 25% now to more than 60%." American taxpayers are headed for a whopping balloon payment on Social Security, Medicare, federal employment retirement, and welfare fiascos. Imagine the future demand for fake IDs—so that all of us young'uns can get in on all those free lunches. Yummee!

—Thomas Winslow Hazlett

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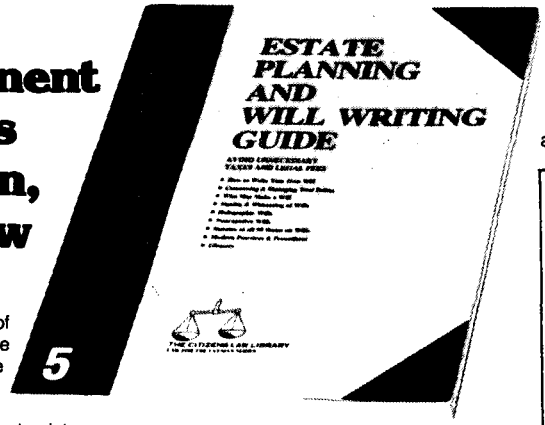

When you work hard most of your life, you certainly want to make sure that your chosen heirs get the overwhelming bulk of your lifelong earnings . . . and that the government's 'take' is squeezed to the absolute minimum.

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- 4 procedures necessary for signing and witnessing valid wills

About the Author

JOHN C. HOWELL, a nationally respected trial lawyer, was admitted to the Florida Bar in 1955 and to the Colorado Bar in 1970. He has also been admitted to practice before all federal and state courts in those states, including the U.S. Supreme Court. Mr. Howell has practiced extensively in corporate law, and has written a number of law review articles. He is also the author of more than a dozen additional books explaining law to the layman.

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Communications Deregulation

"Competition and the private sector shall be relied upon to the maximum extent possible to determine the availability, variety, quality, and cost of telecommunications services, facilities, and products." That statement of policy—in marked contrast to the present "public interest, convenience, and necessity" standard—is the keystone of a deregulation bill that cleared the House communications subcommittee on a 13-1 vote this winter. The bill portends far-reaching changes in the kinds of voice and data services that will be available in the years ahead.

The new standard would make life a lot easier for firms competing with American Telephone & Telegraph in the long-distance market: MCI, ITT, Southern Pacific, and Western Union (whose new "Metro I" service is due to begin at the end of May in 29 cities). But the bill's provisions will also give AT&T something it has long desired: elimination of a 1956 consent decree severely restricting its ability to offer data processing services to its telephone customers. Perhaps because of that trade-off, AT&T chairman Charles L. Brown says the company now "recognizes that competition is a fact of life in our business." The White House is also promoting the bill, having moved telephone deregulation "from the back burner to the front burner," in the words of presidential aide Stuart Eizenstat.

In April the Federal Communications Commission enacted on its own the major provisions of the House bill. By a 5-2 vote it abolished the AT&T consent decree while deregulating entirely the market for terminal equipment—phones, switchboards, data terminals, etc. As of March 1, 1982, phone companies must charge separately for equipment rental and phone service itself, allowing customers the option of renting or buying competing equipment. FCC chairman Charles Ferris commented that the decision "remove[s] the barricades from the door to the information age. . . . Government will no longer be a barrier that prevents or delays the introduction of innovations in technology."

The April move followed an earlier FCC action to increase competition in data communications. Last December it allowed two new competitors—AT&T and Western Union—into the international data market, to do battle with the existing big four: ITT, RCA, Xerox-WUI, and TRT. The latter firms, in turn, are now allowed access to 18 to 21 additional US cities, instead of being limited to five gateway cities. They will thus be competing with AT&T and Western Union domestically.

Moon Treaty under New Fire

The UN's proposed treaty to prohibit private-enterprise exploitation of the moon and other celestial bodies has come under sustained attack in the United States. It is now far from clear that the Carter administration will submit it to the Senate for ratification after all.

While not a single member of Congress has endorsed the treaty, a number have spoken out strongly against it. Among them are Senators Church, Javits, Stone, Hayakawa, and Lugar—all on the Foreign Relations Committee. This kind of pressure has led Carter to appoint an interagency review committee (representing NASA and the Departments of Defense, Interior, and State) to recommend by May 30 whether or not to repudiate the treaty.

A major breakthrough for treaty opponents was the decision of aerospace giant United Technologies Corporation to go public against the treaty. A UTC ad headlined "Stranglehold on the Moon" appeared in February in the *Washington Post* and several New England newspapers. The ad prompted a weak defense of the treaty by Elliott Richardson, US delegate to the Law of the Sea conferences, in a March 24 letter to the *Post.* Richardson's argument, in essence, was that agreeing to UN regulation and taxation—in the seabed and in space—is the price that must be paid for maintaining good relations with the Third World.

The controversy led to articles in both *Time* and *Business Week* in March, as well as a *Los Angeles Times* editorial urging caution on the treaty. At the American Astronautical Society's Goddard Conference, March 27-28 in Washington, a debate on the treaty between NASA's Neil Hosenball (pro) and attorney Leigh Ratiner (con) was won hands-down by Ratiner, judging by audience reaction. It appears, on balance, that private enterprise has a fighting chance to make it into outer space.

Bank Deregulation Brings New Controls

What Congress has given the banking industry with one hand it has taken back with the other. That seems to sum up the financial reform bill signed into law by President Carter on April 1. While removing a number of regulations on banks and other financial institutions, it simultaneously extended significantly the power of the Federal Reserve System.

The bill emerged as a compromise between the House and the Senate. The latter, reacting to court decisions declaring that various forms of interest-bearing checking accounts offered by credit unions, banks, and savings and loan associations were not authorized by existing legislation, sought to simplify financial regulations and give the institutions considerable competitive freedom. The Senate bill called for phasing out Regulation Q (which limits savings account interest and gives a marginal advantage to S&Ls over banks), abolishing state usury laws, and allowing all types of financial institutions to offer interest-bearing checking accounts. The House bill accommodated the latter demand but not the former two.

To break the deadlock, House conferees prevailed upon their Senate counterparts to accept a previously unrelated House bill on Federal Reserve membership. Under the compromise measure, the Fed's reserve requirements will be extended from the 5,600 member banks to some 40,000 financial institutions, vastly extending the Fed's control over money and credit. In exchange, the House went along with the Senate on state usury laws and regulation Q.

Will consumers be better off under the new system? It's too early to tell, but whatever the outcome, the financial community is in for some major changes.

The Economics of Incentives

The idea that incentives really count—and that tax policies can significantly affect productivity—lies behind such tax-cutting measures as Kemp-Roth, Proposition 13, and Jarvis II. And the academic economists who are proponents of this view (called supply-side economics) are increasingly gaining a hearing. Several recent events demonstrate their growing influence.

• Last September economist Arthur B. Laffer unveiled the first econometric model incorporating supply-side effects: the "Prototype Wedge Model." Laffer developed it under contract to the National Council for Capital Formation. The model's equations and its supporting data base provide strong evidence of the link be-

tween increased marginal tax rates and decreased per capita output.

• In February the second such model was introduced by its developer, economist Michael K. Evans. This one was commissioned by the Senate Finance Committee. Among Evans's findings are that (1) a $10 billion tax reduction on income earned on savings would increase people's savings by $13 billion, and (2) a one-percentage-point reduction in personal income tax rates would increase labor force participation (by 0.3 percentage points), raise work effort (by 0.5 percentage points), and lower nominal wage rates (by 0.7 percentage points).

• A March conference on the economy, featuring a broad spectrum of economists and sponsored by the American Assembly, produced such supply-side recommendations as deferring taxes on savings account earnings, lowering tax rates on capital gains, increasing allowable depreciation on new plant and equipment, and steadily reducing the level of government spending as a percentage of the gross national product.

As Paul Craig Roberts summed it up in the *Wall Street Journal*, "supply-side economics is not about to fade anytime soon. With rising energy costs, declining productivity, and tax-flation eating into American living standards, voters and policy-makers are turning to a supply-side view in their search for a new economic policy."

Rescuing New York

No one needs to be reminded that New York State and New York City have become paradigm cases of the folly of excessive government. Since World War II both have expanded their services willy-nilly, borrowed recklessly against the future, and played games with the books to disguise their true financial condition.

None of that is news. What *is* news is that voices of reason are beginning to be heard in influential places, proposing marketplace ideas for rescuing the taxpayers of both the city and the state. The report of the Panel on the Future of Government in New York, appointed by Gov. Hugh Carey, is a case in point. Submitted last December 31, it makes no bones about what needs to be done to restore fiscal sanity to the state. Its major recommendations include:

- effective limits on state and local taxation,
- spending limitations that keep state spending increases *below* the rate of inflation,
- removal of all barriers on government contracting with the private sector for the provision of public services, and
- the organization of public services along commercial lines, with financing based on user charges rather than taxes.

Similar themes of privatization and user charges characterized the annual Richard S. Childs lecture by Prof. E. S. Savas before the prestigious City Club of New York last November. Among his specific recommendations were the following:

- contract out a host of services, from garbage collection to street and park maintenance;
- turn over certain public works—like residential streets and parks—to local civic associations which agree to maintain them in exchange for property tax rebates;
- drop all barriers to entering and operating various forms of surface transportation—taxis, jitneys, vanpools, buses, etc.;
- deregulate day care, to stimulate marketplace arrangements;
- phase out rent controls and public housing, substituting a simple form of rent voucher to aid the poor;
- switch from compulsory to voluntary building codes, along the lines of the French system;
- break the public school monopoly by instituting tax credits and/or vouchers for private school tuition, and end compulsory education for teenagers; and
- revitalize business by drastically reducing regulations and eliminating nuisance taxes.

While these proposals will come as no surprise to readers of REASON, having all been discussed in these pages, they are a breath of fresh air amidst the big-government-oriented approach generally taken by would-be city reformers. Let us hope that New York's movers and shakers take them seriously.

A Rough Draft

While Carter and Congress anxiously push for a resumption of the draft, Defense Department personnel have conceded that their problems would *not* be solved by conscription. The main problem, the Pentagon reports, is *keeping* the men and

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women who have been trained to do highly technical work but are fleeing the services for more-lucrative civilian jobs.

Although all four services last year failed for the first time to meet recruiting goals (the most severely lacking being the Army, which met 90 percent of its requirement), even Army officials say that retention poses more of a threat to military readiness than do mere numbers. Fewer and fewer petty officers and skilled personnel are signing up for the second and third four-year hitch. In the Navy, for instance, 45 percent of middle-level officers signed up last year for a third tour of duty, compared to 60 percent in 1975. In the Air Force, the percentage is down from 75 percent in 1975 to 60 percent last year.

The problem, it seems, is money: military compensation has fallen 12 percent below the rate of inflation since 1972 while civilian pay at least kept pace until last year. Some personnel ease the crunch by moonlighting at civilian jobs; in the Air Force, some 20 percent of the enlisted persons and 6 percent of the officers have outside jobs. At the same time, increasing technology in everyday life is making highly technical skills, such as those of nuclear-rated personnel, a marketable commodity.

Pentagon officials say, however, that conscripts are even harder to keep than enlistees. Forcing a draft would then only compound the problem of keeping trained personnel, especially since conscripts don't have any say in demanding market wages.

But that's not the only problem. An internal Selective Service report predicts that half of the people who would be called to register would claim conscientious objector status if the draft were imposed. The report prepared for the Selective Service Administration by one Donald Guritz, recommends that the federal government draft emergency legislation to eliminate the CO exemption or to "at least" limit it to practicing members of religious sects; that the Selective Service system be the sole judge for CO exemption, subject to no court review; and that those who are granted CO status be severely taxed in lieu of alternate service. "This might include," Guritz proposed, "a property tax taking all property owned in any amount exceeding $500, coupled with an income tax amounting to a virtual forfeiture of all income of more than $5,000 per year for a period anywhere from five to 20 years."

Rep. Robert W. Kastenmeier (D-Wis.) exposed the report at a press conference in March, describing it as a "shocking" inside view that should be officially disavowed by the president. Selective Service claims that the report was simply the opinion of one man—not an official view—and that it was written while Guritz was serving as an Air Force major doing two weeks of reserve duty in Washington.

Congress is currently deciding on whether to appropriate the $13.3 million needed to implement Carter's demand for compulsory registration of some eight million 19- and 20-year-old men and women, and so, in effect, to open up the whole can of worms. The question is, Who's going to defend *us* against the Selective Service system?

Jarvis II Support

Howard Jarvis hasn't gotten over being "mad as hell," and his current campaign to cut state income taxes in half in California (Proposition 9) is garnering more friendly support than Prop. 13 ever did. Among the people appearing in an advertisement plugging the initiative are US Rep. Jack Kemp (R-N.Y.), former Treasury Secretary William Simon, financial author Howard Ruff, economist Arthur Laffer, and assorted California government officials (mostly Republicans). Democrats are keeping relatively quiet because of poll results showing that the Proposition 9 is leading two-to-one and has substantial support in black and brown communities.

An astute commentary by syndicated columnists Rowland Evans and Robert Novak pointed out the real reason for sentiment against the proposition. "It is less a question of undermining government programs because of reduced revenue," they observe; "it is, rather, the threat to undermine redistribution of income through progressive taxation by narrowing the gap between top and bottom rates. Under Jarvis II, California's top-bracket rate... would come down to 5.5 percent. That is the real bite of 'Jaws II.' "

Though anti-tax-cut forces are wary of employing the same disastrous scare tactics that backfired against Prop. 13, Governor Brown has warned of a reduction of 30 percent in the state budget if Prop. 9 passes. Even before the elections, this figure is falling into disrepute. The *Los Angeles Times* reported that the post-Prop. 13 boom in California's economy will add about $1 billion to the state's budget surplus, thus reducing any effects Prop. 9 could have on the budget. And a General Accounting Office report forecasts up to a billion dollars a year in new state revenue thanks to oil price decontrol.

UCLA economists confirmed these projections when they reported the results of their detailed study of Prop. 9's effects: a reduction in state and local government

LAW v FREEDOM

by Anthony Hargis

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It's mind boggling.

M.D., California

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spending of no more than *7 percent* through 1983. Larry Kimbell, director of forecasting at the UCLA Graduate School of Management, added that the spending reduction would occur toward the end of 1981 and decline in the following two years because of the projected beneficial effects of Prop. 9.

The chairman of the No on 9 committee, Mickey Kantor, said that the forecast does not influence his antagonism toward the measure, while a spokesperson for Governor Brown admitted that "we didn't understand all the [economic] complexities when we first called for the 30 percent cut." Note: Brown is no longer directing state agencies to cut 30 percent off their budget proposals for fiscal year 1980-81.

Cutting the Budget

While the bureaucrats spout lofty-sounding balderdash on the need to cut the federal budget, most of them balk at giving any specific recommendations for where it could be cut. Well, one helpful columnist, Robert J. Samuelson of the *National Journal* and the *Los Angeles Times,* has come up with a handy list of generally solid suggestions. Samuelson bases his recommendations on an esoteric document called *Reducing the Federal Budget: Strategies and Examples,* produced by the Congressional Budget Office.

Among Samuelson's suggestions:

- eliminate Amtrak (for a savings of $1 billion in fiscal year 1981),
- jettison the MX missile program ($900 million the first year),
- repeal the Davis-Bacon "prevailing wages" act ($134 million),
- abolish deficiency payments to farmers ($900 million in 1982),
- cut out subsidies of highbrow entertainment through the National Endowments for the Arts and Humanities ($500 million in 1981),
- eliminate operating subsidies of mass-transit systems ($1.6 billion), and
- stop subsidizing the operators of small planes with below-cost user fees ($1 billion).

On the touchier issue of cutting social programs, Samuelson advocates reducing child nutrition programs, pointing out that most of the 26 million children who benefit from the school lunch program come from families with incomes above 125 percent of the poverty line. The savings in this case would be $1.2 billion. Samuelson also takes on Social Security and federal pensions, noting that these benefits rise higher than the earnings of the average worker because they are tied to the Consumer Price Index. Indexing these benefits instead to the increase in average earnings would save from $4 to $6 billion.

There is only one recommendation inconsistent with a libertarian approach and that is repeal of the percentage depletion allowance for oil producers. Samuelson considers this tax break a "subsidy," failing to distinguish between (1) a grant of tax funds (a true subsidy) and (2) merely allowing taxpayers to keep a greater portion of what is already theirs. While the depletion allowance may not be "fair" (any more than deductibility of homeowners' mortgage interest), the answer is not to increase the take from these taxpayers but to reduce everyone else's taxes, also.

Educational Freedom

As public schools further deteriorate and lose their standing as one of society's sacred cows, increasing numbers of parents are choosing to set and meet their own educational standards. According to a report in the *Washington Post,* some 10,000 families throughout the United States are opting out of the public school system and into home education.

The latest court decision regarding home schooling was won in the small town of Dorr, Michigan, early this year. Fundamentalists Peter and Ruth Nobel had decided to take their five school-age children out of both the public school and a local Christian school because of dissatisfaction with the doctrines taught and the standards used. The Nobels derived their religious beliefs from their own Fundamentalist parents and wanted to instill the

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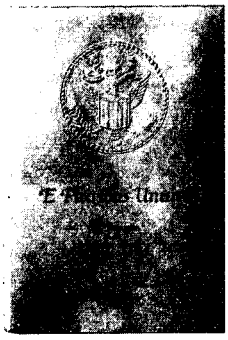

E Pluribus Unum
The Formation of the American Republic 1776-1790

By Forrest McDonald

Having won their independence from England, the American colonies faced a new question of paramount importance: Would this be politically one nation, or would it not? *E Pluribus Unum* is a provocative and spirited look at how that question came to be answered. "A fresh, vivid, and penetrating recreation of the crucial fourteen years in which a new nation was born"—*New York Times Book Review.* "Original and stimulating"—*American Historical Review.* "Highly readable and highly recommended"—*Library Journal.* "Will lead scholars to reassess some of their assumptions about the formative years of the American republic. As one of the most sprightly written brief accounts of this turbulent era it is also likely to gain a non-academic audience"—*Annals of the American Academy.* Hardcover $8.00, Paperback $3.50.

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same convictions in their children.

Ruth Nobel based their case on the US Constitution, which, she notes, "says that government is there to see that citizens keep their rights. The *government* has no rights." After two days in jail for "contributing to truancy," and with the support of a network of religious lawyers and witnesses, the Nobels were judged to be legally exercising their religious freedom. A large factor in the favorable ruling by the district court was the results of standardized tests for learning achievement given to the children by a psychologist; all five girls tested well above grade levels, one by as much as five years.

The Nobels followed the guidelines laid out in a home study course provided by the Christian Liberty Academy in Illinois, one of several sources of such courses (see Trends, Mar. 1979). An interesting twist to the Nobels' triumph is the fact that Ruth Nobel, though qualified, refused even to obtain teacher certification (teacher certification is the only requirement for home schooling in Michigan) on the grounds that "it would have been sacrilegious, giving an honor to the state that belongs only to God. I would not have kept my rights."

The Best Protection Is No Protection

President Carter's overreaction to the Iran crisis is causing uneasiness among Middle East leaders, as well as frustration over his "profound lack of sensitivity to the interests and aspirations of the countries in the region," says a recent UPI report. "We are not afraid of any action by Russia," Kuwait Foreign Minister Shaikh Sabah al-Ahmad al-Sabah stressed. "This is something we are 100 percent sure about. Not only Kuwait, but all the Gulf. You have to know that: 100 percent."

This certainty stems from several factors. One is, except for recent American "politique de spectacle," the internal stability of the region. "They talk about the bases, they talk about sending warships to the area, they talk about the Marines, they talk about nuclear deterrent," a senior advisor to President Shaikh Zayed of the seven-state United Arab Emirates complained. "All of this creates an atmosphere of tension in a region which, in the eyes of

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the people here, is not going through any instability." The decision by the United States and Oman to establish a US base there was publicly denounced by the leaders of the UAE, Kuwait, and Qatar, who worry that this aggressive move may be a dangerous precedent that will only encourage Russia militarily. UAE palace officials say the base, as in the case of Iran, is being set up more to protect the shaky throne of Sultan Qaboos than to protect Oman, which has never been threatened.

Soviet invasion of the oil fields is viewed as a joke in the region. "It simply can't be done," Sulaiman Mutawa, a director of the Kuwait Oil Company argues. "I don't know who dreams up such problems.... Let me tell you, taking over an oil field is not just pushing a few buttons." An American oil man who has been an advisor to the UAE for 10 years points out that the response to a Russian takeover would be widespread destruction by saboteurs. "There are miles and miles of pipeline running across the open desert," he explained. "It is the easiest thing in the world to rip a hole through some pipe with an explosive charge." The oil man adds that both time and money would be lost through such sabotage, since repairs would depend on availability of equipment. The repair of a gathering center in Saudi Arabia destroyed by accident cost $100 million alone. The oil tankers Russia would have to use to get oil back to the USSR would also be open to such harassment.

In addition, the USSR cannot fulfill its own oil industry equipment requirements and last year had to import drill bits and pipes from the West, which would presumably be less amenable in the event of a takeover. Mutawa adds that Kuwait alone has 5,000 trained personnel working on a 24-hour rotation in the oil fields. "They would not be too cooperative to a foreign occupier," he says.

Saudi Arabia is certainly doing fine on its own: donations for Afghan freedom fighters totaled more than $6.9 million in March, with some $890,000 of that coming from the public. A leading Kuwait intellectual, Abdlatif al-Hamad of the Kuwait Fund for Arab Economic Development, summed up the thoughts of most of the region's leaders: "The best thing the superpowers can do for this region is leave it alone. To get out. Because there is little margin for error."

Bad News and Good From China

As reported previously in this department (see Dec. 1979, Feb. 1980), the Chinese are trying to change their ways, particularly in the area of economics. At the same time, Chinese officials seem to be straddling the fence on free speech—at one time encouraging the expression of dissent, and then striking out when the dissent seems too threatening.

Among the more interesting developments on the economic front are the creation of an island of free trade, more state and local autonomy for factories, and the redefinition of capitalists as "working people earning their own living in the socialist society." Planning is under way to make Lang Qi, an island of 72 square kilometers just off the coast of Fujian province, into an autonomous free-trade zone. Fujian's Revolutionary Committee has been working with Bechtel Corporation of the United States and Millie's Holdings of Hong Kong to iron out the details. The government would impose no tax on materials imported for use in production and would keep its hands off all corporate earnings for the first five years; a fixed rate of 15 percent would be levied thereafter. Leases of up to one hundred years would be acceptable, with rental charges at 17 cents per square meter for the first year, increasing by 10 percent annually. The free circulation of foreign currencies will probably be allowed within the zone, as well as the establishment of branches of banks and hotels.

On mainland China, policy has begun to shift from the Soviet communist orthodoxy

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of mandatory State plans and quotas to a more initiative-oriented system. In Sichuan, the largest province, Communist first party secretary Zhao Ziyang has transformed its economy from bankruptcy to progress. Zhao advocates paying people in proportion to their work and has introduced the exciting new concept of income tax—instead of the State's directly taking and keeping most of the person's or factory's output, the person or factory is allowed to keep it and calculate how much is owed in income tax. One hundred factories were allowed to keep their profits last year, to set their own production quotas, and to fix prices for their products. Peasants will be allowed to till privately an increased portion of the land and to determine what they can produce rather than being assigned quotas. Zhao was recently promoted to the six-member Standing Committee—the elite group on top of the Party hierarchy—as part of a general revamping elevating the more moderate members of the Party and purging the more radical Maoist leftists.

And to help strengthen the government's efforts toward modernization, Chinese officials are turning to old enemies. Former capitalists are now being given positions of responsibility. In Shanghai, a former textile mill owner, Liu Jingji, has been allowed to set up the Patriotic Construction Company to help in the economic reconstruction of Shanghai, mainly in housing. Former capitalists "have some experience and some ability in doing business," explains Liu. "We can help improve ways of doing business... and make money year by year." Another capitalist, who has been deputized to head the quasi-governmental China International Trust and Investment Corporation, is millionaire Rong Yiren, whose personal net worth is estimated at $6 million. Rong says that there are about 100 other millionaires in China but that their acceptance into Chinese society does not signal a conversion to capitalism. "We are committed to socialist construction," Rong said, "and while profits have a place in our system, they must benefit the people and the government, not individuals. This is not free enterprise."

In the realm of personal liberty, there is little freedom to be covered up with such rhetoric. China's leading dissident, Wei Jingsheng, was sentenced to 15 years in prison in November 1979. In addition, some 30 to 40 dissidents were arrested for selling transcripts of the Wei trial next to "Democracy Wall." *April Fifth Forum* editor Liu Qing, who also published the transcript, was then arrested when he went to the police station to inquire about the arrests.

Rong was one of the officials who voted to close down Beijing's "Democracy Wall" in February, because, he says, it was diverting attention from economic development. The move was publicly endorsed by the national Central Committee, which further urged the National People's Congress (the Chinese legislature) to delete from the constitution the clause guaranteeing the right of citizens to "speak out freely, air their views fully, hold great debates, and write big character posters." The government is also abridging civil liberties with its massive campaign to limit population growth, using forced sterilization to limit families to one child each.

Despite all this, there may be some political moderation ahead. A new election law mandates 1980 elections of the National People's Congress and of law-making bodies on the county level and below. And in local elections, non-Communists have even been winning. Out of 350 seats in Beijing last year, non-Communists won 130. Democracy is hardly flourishing in China, but it has not been totally eliminated.

Milestones

• *Hour Power.* Two days after the popular television program "60 Minutes" reported on it, the Food and Drug Administration decided to give priority to testing of the drug DMSO. The drug has been barred from approval in the United States despite claims that it can ease symptoms of such ailments as arthritis and shingles.

• *A Public Nuisance.* The Supreme Court has struck down state "public nuisance" laws that allow local authorities in Texas, Idaho, North Carolina, Washington, and Arizona to close down movie theatres showing "obscene" films. Calling such bans a prior restraint of the right to freedom of speech, the Supreme Court indicated that theatre owners may still be prosecuted in a criminal case, although only after the movie has been shown.

• *HEW Blues.* Although Grove City College in Pennsylvania does not receive federal funds, the Health, Education and Welfare Department insisted that it must comply with federal sex discrimination rules. Not so, decided a federal judge in March, chiding HEW for overstepping its bounds.

• *Zipping through Permits.* Land use in Marina del Rey, California is governed by the California Coastal Commission, which is charged with "protecting" California's coastline. The commission rejected a developer's request to build two luxury hotels on the Marina, on the grounds of discrimination against the poor. So the developer changed the plan to provide one moderately priced hotel and another offering a weekend discount to low-income people, selected on the basis of their zip codes. That led to an uproar in the legislature—which in turn caused the Coastal Commission to back down. And the hotels remain unbuilt.

• *Saccharin No Risk.* A study by researchers at the Harvard School of Public Health failed to establish any evidence that the use of saccharin significantly increases the risk of bladder cancer. More than a thousand people were studied, half of whom were afflicted with cancer of the bladder. The study concluded that either: (1) saccharin doesn't cause cancer; (2) it causes cancer to people whose numbers are too insignificant to show up in a study; or (3) not enough time has elapsed since artificially sweetened products were introduced in the 1960s for carcinogenic effects to show up.

• *Steeling Their Bases.* United Steelworkers of America locals 1330 and 1307 sued US Steel for planning to shut down plants in Youngstown and McDonald, Ohio. The suit contended that US Steel made an oral commitment to keep the facilities open. A federal judge has ruled that US Steel can close its works but must keep them in operable condition for 60 days to enable workers to look into the possibility of buying the plants themselves. Youngstown's newly elected mayor George Vukovich lamented: "When you believe in the free enterprise system, it's difficult to have the government interfere and take over." A wiser worker scoffed, "They didn't owe me a job. I made a good living but it was never guaranteed."

• *Sunset for CAB.* The Civil Aeronautics Board is due to self-destruct in 1985, when its few remaining functions will be taken over by the Department of Transportation. It may not be that long, however. Responding to a speech by TWA president C. E. Meyer in which Meyer asked for an earlier sunset, assistant secretary of Transportation William Johnson said "We not only heard you, we think you may be right." Johnson added that a possible sunset date is 1982, after the scheduled implementation of the essential air services program.

• *Price Fixing Booted.* The US Supreme Court ruled that California's fair-trade laws permitting minimum-price levels to be set for alcoholic beverages violate the Sherman Antitrust Act. Thirteen other states have laws permitting the use of price schedules that will be affected by the March ruling.

• *Tomato Protectionism.* A decision by the Commerce Department cleared Mexican growers of charges that they were "dumping" tomatoes and other winter vegetables into the United States below production costs. This convoluted claim was made by Florida vegetable growers, who charge that political motivations (immigration problems and Mexico's oil fields) influenced the Commerce decision and have appealed the decision to the US Court of Customs.

— Robert Poole, Jr., and Christine Dorffi

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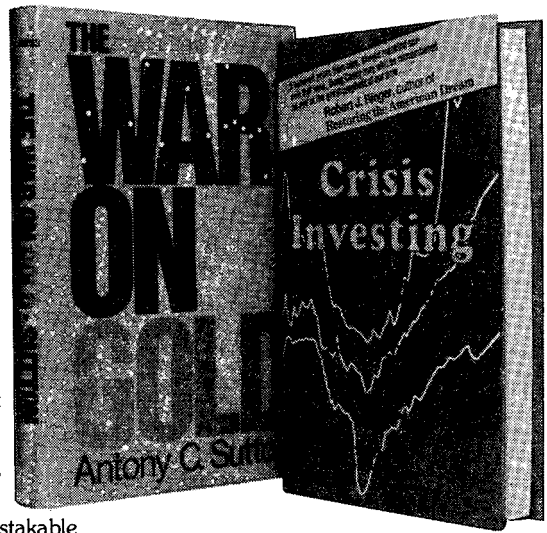

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INFLATION

versus

DEFLATION

Julian Snyder, James Dines, Howard Ruff, and Donald Hoppe debate what lies ahead

Julian Snyder

IT SHOULD BE REMEMBERED, to begin with, that the dictionary definition of inflation is literally an increase in the money supply. That's the number one definition, and if you look in *Webster's,* that's what you'll find. But by an interesting linguistic sleight of hand, government and economic institutions have begun to use the term to refer to an increase in *prices.* And most of us now think of inflation as an increase in prices. It used to be when you said "inflation," that meant literally inflating the money supply. I think that's something that's very well worth bearing in mind.

A second point that I want to make is that it is a mistake to think of inflation and deflation in opposition to each other—like, are you a Republican or a Democrat, rich or poor; are you for or against? Almost without exception throughout economic history, wherever you find inflation you will find deflation. And wherever you find deflation you will find somewhere, hanging around the economic corner, inflation. And sometimes you will find them simultaneously in the same economic situation, and most frequently, of course, you will find a deflation following an inflation.

A quick example: take an increase in oil prices. I've said this many times, and I'm always convinced that at least half the audience doesn't really understand it, but I think the point is very important in trying to define the difference between inflation and deflation. An increase in oil prices is inflationary and deflationary at the same time.

It's inflationary because it increases costs and it increases the bill that the company has to pay or that the individual has to pay and it encourages the increase of other prices. And so that creates an inflationary wave. If you want to get mired in the depths of the chicken-or-the-egg aspects of monetary economics, you can say that the money supply is increased because the oil price was increased, or because the government decided to spend the money stockpiling oil and they had to get it from somewhere so they asked the Fed to increase the money supply; or you can go to the other extreme and say, "Well, the Fed created the money, and that enabled the government to buy the oil." And the Federal Reserve chairman always goes before Congress and says, "I can't do anything because, gee whiz, you guys appropriated the money, and all we do is print it." And then the congressmen say, "Well, well, it's the Federal Reserve that's doing the printing, so they're the culprits." But the important point is that an increase in oil prices, for example, is inflationary because it tends to literally increase prices, and *price* infla-

tion in common terms is what we're talking about.

But an increase in oil prices is also deflationary because it discourages economic activity. The higher you raise a price, the fewer people want to pay it; the fewer people want to pay it, the less activity there is; the less activity there is, the fewer sales, the fewer jobs, the lower purchasing power everybody has. Part of this is the history of the wealth drain by the OPEC nations from the Western world. And that's an important thing to keep in mind.

The other very important thing is that both inflation and deflation are ways of solving a debt problem. Since I don't have a Ph.D. in economics, I gained most of my economic education by studying history, and if you go back and read Adam Smith and before, you find there's a very common pattern of expansion of credit, excess, and collapse that has occurred throughout history. Ever since the banking community discovered that it could lend out more money than it had, there has always been that point at which it could lend out no more. That meant a contraction or a deflation. And you could lend out no more usually because there was a limit to the currency that could be issued based on the fact that somewhere in some vault there was gold or silver or something. Today we don't have that, and somewhere secretly, late at night, there probably are bankers who say, "Hallelujah, brother, print more," because they don't have to worry about that limit.

"Inflationists" know that the banking system and/or businesses and unions and/or the government will print or otherwise create money in an emergency.

The reason some of us are "inflationist" in our viewpoint is simply that we know that the Federal Reserve and/or the banking system and/or the businesses and unions that depend on them and/or the government will print or otherwise create money in an emergency. On the other hand, a sophisticated viewpoint says that, yes, you will get deflationary contractions. That is, when prices get too high, when credit gets too far extended, there will be a contraction.

I think that the question finally is, how do you get rid of excessive debt? How do you get rid of excesses in an excessive borrowing? There are only two ways. One is credit liquidation, which is what happened in the 1930s and in 1907 and in 1873 and in most of the major depressions of history, because, as I said, the banking community reached the limit of its money creation, at which point it had to contract or it had to bust. Or you can liquidate your debts by currency depreciation; so that, while you may owe $100,000 this year at 20 percent rate of inflation, it's really $80,000 next year and so on down the line, until finally you may be paying off your debts in money that isn't really worth very much.

I think it's important to observe in closing that in the great German inflation of 1923 which everyone hears about, and which is referred to frequently by writers, very few people ever say, "And what happened when it ended?" What happened? Was there a deflationary collapse? No, there wasn't. They simply switched to a new currency and went on with the ball game. Meanwhile, all the people who had lost purchasing power during the inflation suffered, but there was not a classic deflationary collapse at that point because it simply was not allowed to happen—although there was great, great economic damage, and Germany certainly did go into a recession.

The next point I'd like to make in conclusion is that in France during the Great Depression they had greater elbow room to create money, and so we had the interesting phenomenon of prices rising in France—in terms of French francs, we had price inflation in France—while throughout the entire rest of the world prices were falling. And the reason was very simple: France was in a depression all right, and France was in economic trouble and France perhaps was worse off than many another country, but France was able to run the printing presses.

So in arguing these two cases I think that the thing to look at is the practical aspect of the thing. And from a practical point of view, our government and their agencies and the Federal Reserve have the option of printing or otherwise creating money. And they will do so if and when the emergencies come.

James Dines

THIS IS A VERY IMPORTANT, vital debate. Why? Because it affects your strategy over the next months and years. If a hyperinflation is due to come, then the wise strategy will be to borrow heavily to buy common stocks, to be negative on gold stocks because their costs after all are a function of inflation, and to sell bonds. On the other hand, if you see deflation coming, then you should pay your debts off now with cheap money, buy gold stocks because their costs would decline, and buy bonds at the coming interest rate peak. So this is a very, very vital debate within the honest-money movement itself.

I want to stress that everybody debating here agrees that a deflation is coming. The question is, when? You see, if we have a deflation very soon, then you should begin taking deflation strategies immediately. On the other hand, if it's coming after the next cycle, then you should take an inflation strategy. And therefore this is a very vital distinction. What I'm saying is, Don't tell me what to buy; tell me when to buy it. So the debate within our movement is on timing. And I believe, therefore, that the killing question is, Will inflation accelerate first?

Now it's tempting to say yes. Why? Because with the argument that you create more and more money and you have more money chasing the same goods and the fact that the Keynesians are still in charge, it's very easy to say that inflation will continue and actually accelerate. Yet when all think

alike, nobody is thinking very much. What is everybody overlooking?

To get a deflation you need a contraction in the money supply. Without a contraction in the money supply, a deflationary argument fails. Now, as an intellectual exercise, what could contract the money supply? One, it must be a surprise; otherwise there would be no debate such as ours where all these very intelligent people disagree. Two, all previous inflations ended by surprise, such as late 1929. Even now, very few people agree on why 1929 occurred, so we are dealing with an inherently surprising phenomenon.

Some people say, "Well, the government's going to print more"—but there aren't enough trees in America to print that much paper!

Now I predicted earlier a debt-liquidating depression. Whom do you know who has actual cash on hand in a safety deposit box earning interest? The odds are, very few people. If the market moves generally to foil the majority, the time is ripe to destroy those who are overextended in debt. The situation in Iran could trigger a sharp but temporary oil price boost. How about $100-a-gallon gasoline? *Something's* going to have to break. It's unreasonable to assume that the Arabs will continue taking all that paper. Somebody's going to have to go broke on this type of thing.

It's hard to say where it'll break. One of the things that must occur is a sharp drop in the Dow Jones industrial average. We must get a drop below 570.01—which is the December 1974 low for the Dow—or my Dines gold contracyclicality theory is worthless, and it is *not*—it is one of the great principles of the market. Now, a sharp drop in the Dow Jones will contract the collateral of those who have borrowed on stocks. In other words, IBM is now, believe it or not, the same price it was 10 years ago. So if IBM has a good drop, all those people who borrowed on it will need to raise more cash. But from where? Where are they going to get cash? So that's why I say, cash will be king.

The coming scramble for liquidity will be the opposite of what has occurred in the last 30 years, where people have generally fled from cash into things, into collectibles and the like. So we're getting now a change, a shift in polarity. Now that the whistle's being blown, the game's changing. Instead of going from cash into things, now we're going to go from things into cash.

Let's say, for example, we have a failure in a less-developed country. They call them LDCs. I personally call them LDBs—less-developed bankrupts. I include New York City, of course. There's no way that these countries overseas can pay off their loans; they don't even have enough money to meet the interest payments. So the question is, When will it be recognized by the banking system that those loans are worthless? Some big banking failures have come along by surprise, and a spark could start a wave of bankruptcies. After all, when a bank is going bankrupt, the first thing they're going to do is go through their loans and say, "You—we're not going to renew your loan," or, "You—we want your money back right away." And where are you going to get cash? So this is part of the scramble for liquidity.

The most important part of my argument is that when you count the actual dollars in this country, there's only a hundred billion of them—that's actual green dollar bills and coins. That's it. The rest of the $400 billion money supply is all in the memory cores of computers. You've got a bankbook, but you don't have money—you've got a little book that *says* you have money. That's the strict truth. So, if a bank goes broke and fails to pay its electric bills, they'll pull the plug in the computer and the money's gone. It disappears overnight. And that's what we're going to have. I think we're going to see the worst, the most incredible, contraction in the money supply in history.

Now, some people say, "Well, the government's going to print more." Listen, there aren't enough trees in America to print that much paper! They say, "Not *me*. My money's in the bank, insured by the Federal Deposit Insurance Corporation of America." And I ask, "How much money do you think the FDIC has on hand to meet its potential liabilities?" Most people have no idea. It's *three percent.* People aren't ready for what's coming, let me tell you.

Since 1966 I've said there will be no hyperinflation. We are going to have an inflationary evolution that will evolve into a deflationary crash. Those who are prepared are going to survive; those who are not, will not. And I wish to be of service to you by warning you that this is coming. I said we would have an inflation; we've had it. I said the stock market would go nowhere; we've had it. Now the only thing that remains is for deflation. It's the final stage of my prediction, the last piece to fall into place.

You can ignore me, and then after deflation you'll be saying, "You're right." But I don't want to be right; I want to help you! Listen, my predictions are already a legend on Wall Street. I don't like to miss. There's no hedging in my prediction. I see a great deflation.

And remember this: gold is not an inflation hedge. People now understand the function of gold. Gold is going up not because of inflation but to anticipate the deflation that's coming as it did in 1931.

Howard Ruff

NOT TOO LONG AGO Dr. Hans Sennholz sent me a copy of an article that he wrote once and thought I'd be interested in. It was called "The 39 Dirty Tricks of Debate." Jim Dines just used six of them, and I'm going to use the other 33!

I'd like to ask a simple question. Everybody's against inflation—conservatives are against inflation; the liberals are against inflation; even Teddy Kennedy hates inflation. So if everybody's against inflation, why don't we stop it? Good question?

Maybe the most important question asked here tonight.

Well, I think the reason's pretty simple. We're having more inflation because, even though we all hate it, the majority of the people in this country have a stake in the programs that are causing it. Fifty-six percent of the people in the United States receive a check from some level of government. *Fifty-six percent.* And if you add up the Social Security recipients and their dependents, welfare and their dependents, Aid to Dependent Children and their dependents, military and their dependents, military retirees and their dependents—which does not include the defense contractors and their employees and their dependents and their suppliers and their employees and their dependents and all the little businesses that operate around and live off of them—it actually comes to about 73 percent of the people in this country. It is often said that democracies are in the state of final decline when the majority of the people discover that they can vote themselves benefits from the public treasury. And it is a massive majority.

Now, I'd like to make a very careful distinction and definition of inflation. I agree with Julian Snyder. Inflation is defined in the dictionary (and it still is a darned good definition) as increases in the money supply, over and above the available goods and services. If you define inflation as increases in prices, you will immediately start fighting the wrong problem. That's the kind of thinking that has the Carter administration fighting inflation by attacking wages and prices, which is sort of like doctors fighting diseases by pressing for a local ordinance to control thermometers so they won't go above 98.6 degrees, while quietly encouraging the spread of virus A throughout the community. If you think that way about what inflation is, you'll come up with the wrong answers; and you'll come up with the wrong conclusion about where we're headed, because you can build a perfectly rational scenario for deflation if you come up with that twisted definition. So let's take a look and see how inflation happens, but first, a couple of quick points.

First, the argument that you hear from the deflationists basically adds up to the final conclusion that inflations are impossible. They describe events that have occurred in every major runaway inflation since the history of paper money—and call them deflationary. But if you argue that inflations are impossible, then I wonder what it was that they had in Germany between 1919 and 1923.

Second, their argument often is that credit collapses are deflationary; that rises in prices generally bring rising long-term interest rates, which means falling bond markets, shrinkage of purchasing power, etc. That means bankruptcies, and all of the money supply that exists in the form of credit disappears. Well, that happened in Germany in the early stages of their runaway inflation, but it was not deflationary. All it did was create a tremendous demand for paper to supplant credit. We have a credit economy. There is a process by which you go from a credit economy to a printing-press economy.

All the things that appear deflationary will ultimately be inflationary, because all the fire extinguishers are loaded with kerosene.

Point number three: If you are arguing that there's going to be a deflation, you are arguing that paper money will become more valuable, because deflation is an increase in the value of paper money. But I find that history records no example of a major inflation by a dominant civilization that ever resulted ultimately in an increase in the value of its currency. I just don't think there's any precedent in history for that argument.

Now, inflation is an increase in the money supply, but not the money supply as it is commonly defined by *M*1, *M*2, and all the other *M*s. I believe that an increase in money market funds is an increase in the money supply. I have money in a money market fund; our corporate funds are in there. We treat it as an interest-bearing checking account, but when we took our money out of the bank to put it in the money market fund, the figures showed a decrease in the money supply. Was there really a decrease in the money supply? T-bills are part of the money supply. People treat them as the equivalent of cash, and when the money market funds buy them and you buy the shares of the money market funds, you really have money. So in my opinion the money supply is really increasing at a faster rate than the figures show.

When interest rates rise to compensate long-term bond holders, long-term lenders, for the increasing loss of purchasing power of their bonds, bond markets fall. You have a credit collapse, creating a need for more cash, as I indicated. You do get recessions in an inflationary cycle. We're going to get one—it's going to look for the next 6 to 18 months like all these guys are right. It's really going to look like it, because we will have a temporary deflationary scenario.

Jimmy Dines said there aren't enough trees in the country to print enough money. I say, if you put enough zeroes on a bill, you could print it by cutting down the trees in Central Park. When you start getting everybody in trouble and all these deflationary things start happening, is Uncle Sam going to stand there wringing his hands saying, "Bankruptcy"? No! They'll do what they have to. They'll change the bankruptcy laws so nobody can do it. They'll declare a moratorium on debt. The banks will realize that they can't let everybody go bankrupt—*they'd* be bankrupt. So they'll stop calling loans. In my opinion, they won't let it happen. I think they'll freeze everything until they can print enough money and rush it to the rescue. And all the things that appear deflationary will ultimately be inflationary, because all the fire extinguishers are loaded with kerosene. They'll do what's necessary until they can rush that money out there, because they've got to inflate or die. Inflations are *caused*, and I believe they've got the tools to do it. They can create money in any amount and they've got a number of sophisticated ways to do it. They could go to a totalitarian government and freeze prices for a while if they have to, until they can rush the money out there.

Now, I believe that eventually it becomes a psychological phenomenon, just like it did in ancient Rome, where people say, "I don't trust that money. I don't know how much base metal they mixed in that coin. I want more of it in return for my goods and ser-

vices." People refuse to accept credit. They won't extend credit. Why? Because they know they'll get paid back in cheap dollars. They'll say, "I want cash." It creates a tremendous demand for cash, and then they've got to go to the printing press. You move from a credit economy to a printing-press economy. History records no example of a dominant civilization reaching the levels of money creation that we have without its running its course in a deflationary or an inflationary depression.

Now let me make one point. I think you can have an inflationary depression. Most depressions are considered synonymous with deflation. I redefine depression. Depression is a massive loss of purchasing power throughout the community. You had it in the '30s because prices fell but wages fell much faster and 25 percent of the people were out of work. There was the real loss of purchasing power. And you can have it in inflation because prices can rise much faster than incomes, and there is a massive loss of real purchasing power throughout the community. My opinion is that that is what we face, and I agree with Julian Snyder that what we will have at the end of that is not a deflation—which again, remember, means money being worth more. The psychological damage to our money will be absolutely irreparable. No one will want to trust it. Where is the German Deutsche mark of 1923?

So, what will happen? In my opinion, we will have a new currency, a new kind of a system; maybe a couple of wild attempts to find some currency the people will trust, fiat currency—"This is money, or else!" In France during the Great Terror they beheaded people if they didn't accept it, and people were beheaded because they wouldn't. And then sooner or later they will be forced, literally forced by circumstances, to come up with a gold-backed currency that people will trust. That is the day when sanity will be restored, and it will be a brand-new system unrelated to the previous one.

I do not believe that deflation is really possible. Although I am still prepared to bet on a short-term, mildly deflationary scenario, I believe that the long run is more and more inflation. And Jimmy Dines is right—it's a crucial issue, because if you don't get it right you'll bet wrong with your money, and you will lose.

Donald Hoppe

I THINK WE SHOULD DEFINE AGAIN. Everybody's defining inflation, deflation. Let me add my definition. Inflation, as I understand it, is simply a decrease in the value of money, and deflation is an increase in the value of money. Now we can't talk about the classical definition of inflation—as an increase in the money supply—because we really don't have any money supply any more. As somebody pointed out, our cash currency and coin is a very small, insignificant part of the money supply, probably something less than five percent. Ninety-five percent of all payments are made with some form of credit. Now you can't say credit is money—not and understand economics. No one can define credit as being money. Credit is a loan of money, not money in itself, and it accounts for 95 percent of all the payments we make.

Now let's look back historically. I agree with the inflationists that if you look back over a long period of history you will find that the normal condition is a moderate inflation. Episodes of deflation and episodes of hyperinflation are relatively rare in history. It's a very unusual phenomenon. You can count the very few examples of hyperinflation on your fingers—the German inflation of 1923 that everybody refers to, the *assignat* inflation in France, inflation of the Continentals. You can also count the episodes of deflation on your fingers. They're very rare occurrences that only last a relatively short time.

So I'll agree that over a long period of time inflation is the rule, not the exception. Nevertheless, as Keynes used to say, in the long run we're all dead. And our fortunes are made not in the long run but in the short run. The deflation of the last period, 1929-33, only lasted three years; after 1933 it started inflating again. But the damage was to most people who lost their property in 1929-33; they lost the savings of a lifetime in that period. So you have to guess right on these short periods of time. The same goes for the runaway inflation in Germany from 1919-23—a very short period of time, relatively; only three years. So we can't talk about inflation or deflation as something that expands over a long period of time. We're talking about something that happens in a very short time. But that very short time is enough to ruin you.

I would say that conditions right now suggest very strongly that in the next few years, maybe not more than two or three years, you're going to have a severe deflation. Now, after that you have a resumption of the moderate inflation that is typical of history. But you see, if you get caught in the short-term deflation it won't matter that there's going to be inflation in the next seven or eight years. You won't have any money anyway. So we have to guess right.

Now, I agree again that any government would like to keep on inflating forever. It's a great system. But right now we can't. The people debating here act as if the United States is a completely isolated country in the world, that we don't have anything to do with foreign countries. But of course that's nonsense. It's one world, as Wendell Wilke used to say. We're totally dependent economically on other countries. We cannot conduct our financial policy independently of other countries. If we depreciate our currency further, the price of oil is going to rise. They've already told us that. Now in the last 10 years we've gotten by in this country, not by inflating, but by borrowing. Whom have we borrowed from? We've borrowed from foreign countries. We've borrowed from the Germans. We've borrowed from the Japanese. We've borrowed from the Arabs. We've borrowed from everybody else. Now, if it can be proven to me that foreign countries are going to be dumb enough to keep on loaning us money forever, I'll concede that inflation will continue indefinitely. But I don't think they're going to be that dumb.

In fact, they already told us they're not going to loan us any more money. We got $30 billion from them in November 1978, and by July 1979 we were back where we started from. We spent the $30 billion, and the dollar was lower than it was when we borrowed it. I think Mr. Volcker went to Belgrade looking for another handout, and they told him there wasn't going to be any more handouts. Sheik Yamani, the Arab oil minister, says that if the dollar keeps going down they're going to suggest switching to some other currency. And if they do, we're going to have to buy our oil in the spot market, where the price is considerably higher than the official OPEC price. We're importing 50 percent of our oil right now, and without oil there's going to be the worst depression you ever saw, with industry shutting down all over the country. So you can't do what you want. Our foreign policy, our financial policy, is not being made in Washington today. It's being made in Saudi Arabia. It's being made in Bonn. It's being made in Japan.

So we're in a crisis situation where we simply cannot inflate. Not that we wouldn't like to bail everybody out, but we can't do so. If we attempt to do so we are simply going to start another panic run on the dollar, and we're going to be cut off from our very essential trade with the rest of the world. We import not only 50 percent of our oil but a whole host of vital industrial materials. In order to buy something, you have to have good money to pay for it. And if you depreciate your own currency, you don't have any good money. Of course, they do it in Argentina, they do it in Brazil; but in 1978 Argentina had an $8 billion surplus in their foreign accounts, and we had a $40 billion deficit—that's the difference. And we cannot keep inflating because our deficit will simply get worse, and they'll cut us off the first time we try it. The price of oil is going to go right through the roof. And the price of oil is the single most important thing today for the American economy. This economy runs on oil. It shouldn't, but it does. If you think Chrysler's going bankrupt is bad, think of all the other industries that are going to go bankrupt if they don't get a steady supply of oil. You'd have the worst chaos in the world if you tried to inflate today.

Now everybody points to the example of Germany in 1923. But to go back 50 or 60 years and look for an example of inflation in a totally different historical context is really, really unfair; it's an unsound argument. The Germans inflated in 1919-23 for one reason only—they wanted to get out of paying the reparations. And they did. In fact, they borrowed more from us than they actually paid in reparations. The Germans admit in their memoirs that the inflation of 1919-23 was a put-up job so they could get out of paying the reparations.

With World War II, the destruction of Germany was far greater than with World War I, and there was no runaway inflation. Why? Because there was no advantage to it. The old Reichs mark of Hitler was exchanged for the new Deutsche mark at only ten to one—which is no worse than the dollar is today. Ten to one, as opposed to a trillion to one after World War I.

Prove to me that foreign countries are dumb enough to keep on loaning us money, and I'll concede that inflation will continue indefinitely.

So runaway inflations, like deflations, are very rare things and only occur under unusual situations. And there's not going to be any hyperinflation in this country. If there is, we might as well throw in the towel right away, because the American economy will collapse.

And if the American economy collapses, the Russians will be washing their socks in the Atlantic in 48 hours. They're sitting there waiting for the American economy to collapse. So runaway inflation at this time would simply be an act of national suicide. We are not alone in the world. We exist in a world of very frightening forces with a powerful opponent out there waiting to knock us off. And if we simply think we can buy our way out of this with a printing press, that's crazy. You can't do it—not unless you want to commit suicide.

One more thing. The bond market in this country is 10 times the size of the stock market. And if you inflate, what happens to interest rates? They go up. If interest rates go up, what happens to bond prices? They go down. You could have the worst financial crash in history, 10 times the size of the stock market crash in 1929, if interest rates keep going up. Already, bank portfolios are jeopardized by high interest rates. Has anybody tried to sell a bond lately? You can call up your broker and tell him you've got 100,000 bonds to sell and see what kind of a bid you're going to get. You may not get any bid at all.

So we definitely have the potential for a deflation. We have a credit economy; we have an enormous amount of debt outstanding in the form of bonds, and mortgages, and consumer installment credits, that could be wiped out by further inflation. Inflation is a self-destructive phenomenon, a self-limiting phenomenon—the more we inflate, the more we ruin our credit markets. It's not a question of replacing the credit with paper. You can't do it that way, because if you print more paper you drive interest rates up, and if you drive interest rates up you destroy credit. Whose credit are you destroying? Our credit; all of ours. We all have insurance policies. We all have bank deposits. We all have money market funds. We all have credit. As I say, 95 percent of our financial assets are in some form of credit. And rising interest rates destroy all these assets. It devalues them. Every one percent that interest rates go up, a $1,000 bond goes down $100.

That's why inflation will *have* to be ended. And that means a period of deflation. ◻

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SECOND IN A SERIES

FTC Flaw

Investigation uncovers fact that FTC unable to stop fraud. Real purpose of agency? Serious doubts raised.

FIRST OF A SERIES

FTC Revolt

You've heard of the tax revolt. It's about time for an FTC revolt. Here's my story and why we've got to stop federal bureaucratic regulation.

Here's the story of my continuing battle with the FTC and how I uncovered a major flaw in their performance. The ad shown here was the start of my campaign.

By Joseph Sugarman,
President, JS&A Group, Inc.

My lawyers thought I was crazy. Here I was under investigation by the FTC for violating their rules, and I was making plans to run the advertisement shown above.

The advertisement explained how I had shipped products late as a result of a series of 1979 Chicago blizzards and a computer breakdown. It explained how the FTC accused me of violating their rules, and how they tried to force me to pay $100,000 with threats of a massive subpoena and a long legal battle that would cost my company more than the penalty itself. As one attorney put it, "It's like a bully pulling out a gun and saying, 'If you don't give me a nickel, I'll blow your knee caps off.'" He said the fight wasn't worth it.

WE REFUSE TO PAY

But I refused. Although I admitted that we did ship some products late, all products were shipped and not one consumer lost a penny. I also accused the FTC of applying their rules to legitimate companies while leaving the real rip-off artists alone.

The advertisement also told Americans to write their congressmen urging them to take the powers of the FTC away from the unelected bureaucrats and give them back to our elected representatives.

Before I ran the ad a few of my friends, who knew how the FTC operates, told me that if I ran the ad the FTC would triple their efforts against me. The FTC did. They told me that the FTC would discredit and smear me in the press. The FTC did.

CAMPAIGN SUCCESSFUL

The ad campaign ran in hundreds of publications and started an outpouring of mail—Americans writing Congress urging their legislators to stop our national bureaucratic abuse. Partially as a result of our efforts, Congress reacted overwhelmingly by supporting bills in both houses to control the FTC.

It is now over a year since the start of the FTC investigation of our company, and the FTC has still been unable to prove a case against us. Our massive advertising campaign not only made our case public, but would have certainly generated an outpouring of complaints against us, if indeed there were any.

Even more serious however, was a discovery we made while trying to convince the FTC to get off our backs. I was in the office of the FTC's head of the Bureau of Consumer Protection in Washington. I asked him why he did not go after companies that do defraud the consumer, when my company, a highly respected firm, did not defraud anybody.

He said, "We're not set up to deal with real fraud." This supported what I always suspected, but I never expected the head of the Bureau of Consumer Protection to admit it so openly. Incidentally, this statement was later confirmed by a high-ranking FTC official. Yes, the FTC is not set up to go after companies that purposely defraud the consumer.

SERIOUS FLAWS

This leaves me with serious concerns for our free enterprise system. If an agency responsible for the protection of the consumer is ineffectual against the real frauds, yet goes after the legitimate companies, then they are deceiving Congress and the public.

First, the FTC is permitting the real rip-off artists to continue to plague the consumer totally immune from their rules.

Secondly, they are undermining the free enterprise system—the same system they are suppose to protect and encourage—by concentrating their efforts on firms such as JS&A which are trying to serve the consumer and who may unintentionally err and violate one of their rules.

Ironically, they point to statistics which show a rise in mail order complaints as a good reason for their stiff rules, yet their rules are totally ineffective against the companies that cause most of those complaints anyway.

I WON'T GIVE UP

I am an American small businessman—an entrepreneur who started my company in my basement eight years ago, and through a lot of hard work built it into one of America's most respected electronics marketing companies.

I refuse to let my reputation be slandered and discredited by a few publicity-seeking bureaucrats whose efforts attack legitimate companies, thus undermining our free enterprise system, while leaving the crooks free to rip-off the unprotected American consumer. And it's the consumer, footing the bureaucratic waste, who thinks the FTC is doing a good job and needs to be strengthened.

INVESTIGATE THE FTC

I urge Congress to conduct a thorough investigation of the FTC. If they are indeed not set up to go after the fraudulent companies, and if indeed they have been unnecessarily harassing small businessmen, the FTC should be severely reprimanded. I am not for the elimination of the FTC. Quite the contrary. I am running this campaign to help a sick agency so that Americans can get the protection they think they are getting while allowing the free enterprise system to function without bureaucratic harassment.

Every American can help me in my battle. Tear out this ad and send it to President Carter with a personal message. Tell him to insist on an investigation of the FTC and their tactics. President Carter, a small businessman himself, has indicated his desire to help small business and eliminate bureaucratic waste. Remind him of his promise.

I guarantee you, I will continue to fight my battle by running this advertisement throughout America until the FTC is investigated and put back on the right track. I don't want contributions, but if there are magazines and newspapers with the guts to stand up with me and run this ad, let me know and I'll send you a printing plate. I'll need plenty of help.

If I can correct the FTC, I will have accomplished more for my country and its consumers than many of the FTC's misguided efforts.

Freedom is not something that can be taken for granted, and you must often fight for what you believe. I am prepared to lead that fight.

Note: For more details on my particular case and a further guide on what action you can take, write for my free booklet, "Blow Your Knee Caps Off," at the address below.

JS&A® PRODUCTS THAT THINK®
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A Unique Service

New Publication Promises Investors an Edge in the 1980's.

by William Bonner

Mark Hulbert is one of a new breed. A "whiz kid" with a degree from Oxford University, Hulbert is convinced that too many investors "fly by the seats of their pants," and lose millions as a result.

"They tend to follow the advice of one investment advisor without any way of judging the quality of the advice," he says.

Hulbert, author of numerous articles on international finance, has spent years researching banking practices and economic trends. He decided to put his research abilities to work scrutinizing the investment advisory services.

He started a gutsy new service, with a new publication, called the *Hulbert Financial Digest,* at its head.

The maverick publication digests the advice of other financial experts—including well known experts such as Julian Snyder, James Sinclair, T.J. Holt, C.V. Myers, Howard Ruff, Harry Schultz, and many others. It presents a summary of the advice offered along with an analysis and commentary from the editor.

In effect, the reader gets *thousands of dollars worth* of financial advice for the relatively low price of $37.50 which Hulbert is charging his **CHARTER** subscribers.

That alone would seem to make the *Hulbert Financial Digest* a sure winner among hard-pressed investors of the 1980's. It virtually guarantees investors access to the best investment advice around at a very modest price.

But Hulbert doesn't stop there. The *Hulbert Financial Digest* also keeps track of the advice each expert is giving and *rates them on the basis of their performance.*

Investors can check their own investment strategies against those of the experts on a regular basis. They can see which strategies are paying off and which are not. (Hulbert even goes so far as to give dollar amounts for the success or failure of the various investment strategies he analyzes.)

"Another problem with much so-called investment advice," says Hulbert, "is that it is nothing more than vague generalities about the state of the economy. Several of the investment letters I analyzed gave absolutely no concrete recommendations."

Hulbert has a solution to this problem too. His new newsletter will rate financial advisors on the clarity of their advice as well as the information they contain.

"This is a way to make sure the investor gets his money's worth," says Hulbert. "We'll tell them when the advice can be translated into profit...and when it can't.

"Also, the *Hulbert Financial Digest* will distill huge amounts of verbiage into a simple, straightforward summary. This will enable the busy executive to get the most useful information in the least amount of time.

"The investors who subscribe to my newsletter," Hulbert pointed out, "have a clear advantage over those who do not."

The first issue of the new publication is scheduled for July 1980. Already, demand for the new service has exceeded Hulbert's own expectations.

The demand is partly explained by the **iron-clad guarantee** Hulbert is offering.

"If anyone is not completely convinced that this publication is a great benefit in choosing the most profitable investment strategy for the 1980's, after they've received one issue, I'll refund every penny of their subscription money. No questions asked."

This guarantee allows curious investors a chance to try Hulbert's publication *without risking a penny.*

"It would be foolish for an investor not to give this offer a try," Hulbert maintains. "The average investor has thousands and thousands of dollars at stake."

"If it turns out that my service can't help the individual investor, he just cancels and gets all his money back. It doesn't cost him a dime."

"On the other hand, if this service is as valuable as I think it is, the investor stands to make thousands of dollars over the next few months with an investment of just $37.50."

Investors who want an edge in the 1980's are invited to fill in the coupon below and mail it to *Hulbert Financial Digest,* 10 E St., S.E. Washington, D.C. 20003.

I'd like a Charter Subscription to the *Hulbert Financial Digest.* I understand that I may subscribe at *half-price* and that I may cancel after receiving the first issue and receive a full refund, if I'm not completely satisfied.

☐ Enclosed is my check for $37.50.

☐ Please bill to my:

Mastercharge _____

Visa _____

Exp. date: _____

Name _____

Address _____

City _____

State _____ Zip _____

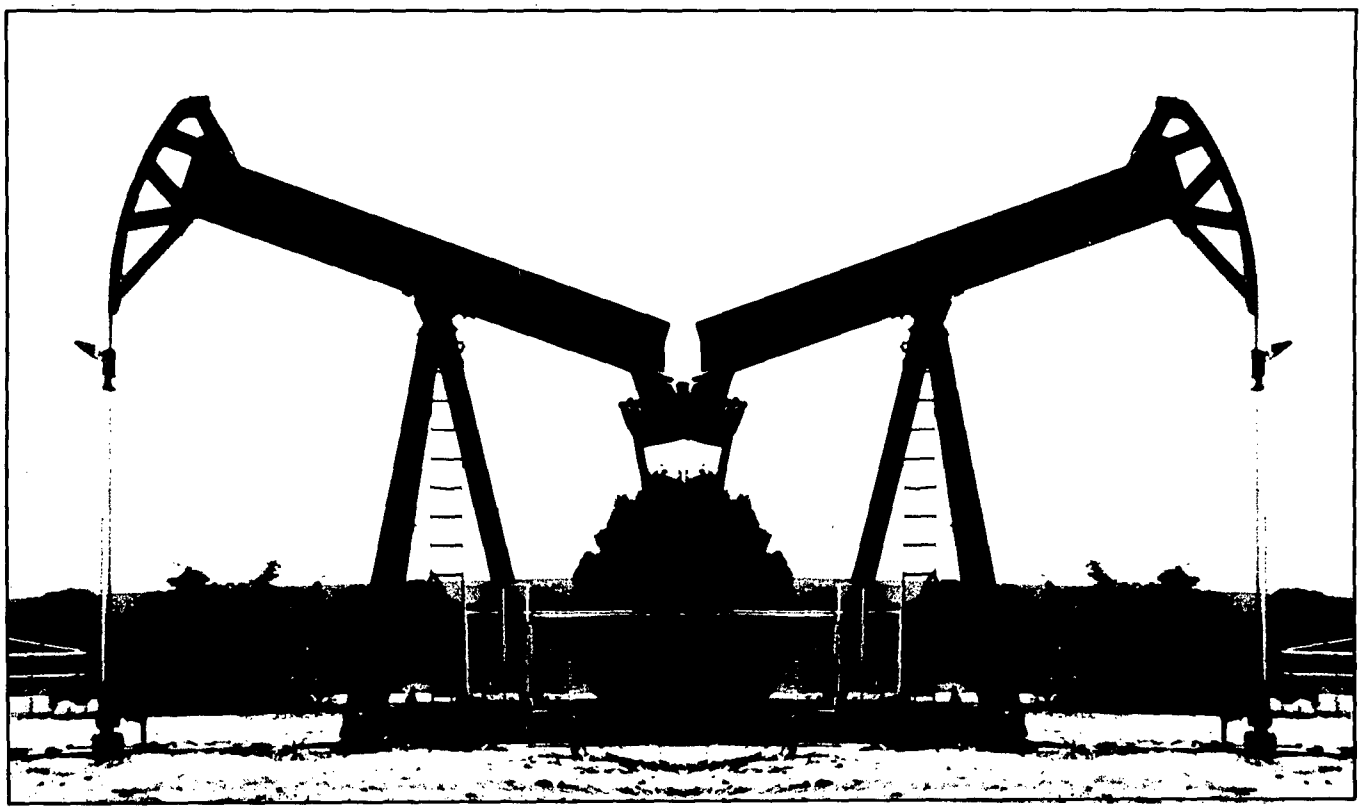
OIL AND GAS BETTER THAN GOLD

E. Raymond Pastor

GOLD COMMANDS a greater value in the marketplace today, so there is obviously more incentive to produce it. Even with production costs of $300 an ounce, it has become economical to reopen old, boarded-up mines in gold-rich Nevada and Arizona. So it is with crude oil and natural gas—but even more so. Gold will fluctuate violently in price and may even slip back to $300 or $400 an ounce. Oil and gas reserves in the ground, on the other hand, are more likely to continue to command increasingly higher prices in the world marketplace.

Oil and gas possess excellent investment merit today primarily because they are such vital and universally *essential commodities.* Civilization, for the foreseeable future, literally cannot go on without them. Surely jetliners are unlikely to fly on nuclear energy cells for some time to come, and cars are not going to run on sunshine!

Global oil consumption is presently 23 billion barrels annually. The crude oil reserves for most OPEC countries continue to decline rapidly. For nearly a decade, America's proven reserves of oil and gas have also continued to decline. If the non-Communist-world demand does no more than maintain the status quo over the next decade, 200 billion barrels of *new oil* would have to be developed to maintain proven reserves at the present level.



The classic supply-demand imbalances that have created spectacular price explosions in the past clearly exist in oil and gas today. Is $100 a barrel really unthinkable? Was $800 gold? Just a couple of years ago it was indeed. Can't we assume, with a high degree of confidence, that there is the likelihood of continually rising prices for crude oil and natural gas perhaps throughout this decade?

BULLISH ON OIL

Imagine, if you will, what existing reserves in the ground would be worth today if there were widespread fears that no new significant provinces of oil and gas were to be found! Those who *owned* reserves would enjoy a windfall of inestimable scope. The truth is that, despite an intensification of exploration worldwide, major oil discoveries of late have been relatively few. Important finds have been made in the Canadian Arctic, Libya, Mexico, Nigeria, and Red China. Lesser oil strikes have been made off shore Brazil, India, Malaysia, and Norway.

Despite highly intensive exploratory effort during the 1970s, outside of Mexico no *major* oil and gas province was discovered. Numerous optimistic forecasts of substantial new reserves of oil and gas were unrealized. The immense oil and gas provinces in Alaska and the North Sea were discovered in the 1960s. Only recently have important gas discoveries in the United States been made in the Overthrust Belt of the Rockies, the Tuscaloosa Trend in central Louisiana, and in the Gulf of Mexico.

The point of this background is to impress upon you that the easily discoverable and recoverable oil has already been found. Look at where the major exploration and development activities have been going on of late: the Arctic Sea! Alaska! the North Sea! offshore Newfoundland! Each location is most inhospitable and extremely expensive to develop. In fact, the investment required to bring on production a daily *single barrel of oil* runs about $10,000.

Soaring prices for crude oil, in conjunction with declining reserves, have spurred unprecedented expenditures for new exploration and development. Capital requirements for the entire non-Communist oil industry have been forecasted to rise from over $20 billion this year to at least $70 billion by the end of the century. The anticipated acceleration in outlays will substantially exceed that for all industry in general.

The rapidly rising prices for crude have rendered the prospects for natural gas significantly more favorable, too. Previously uneconomical pipeline projects, requiring multibillion dollar investments, are now feasible. With 5.3 thousand cubic feet of natural gas equivalent to the energy output of a single barrel of oil, and the sharp escalation in fuel prices, there has been accelerated drilling for natural gas.

What this all means is that oil and gas reserves are an outstanding investment opportunity in this decade of energy crises. Geographic and climatic factors point to continuing price escalation and restricted availability for oil in this decade. Oil and gas reserves in the ground are likely to become increasingly more valuable. Those who recognize this opportunity, and are cognizant of the best ways to capitalize on it, will profit handsomely.

Those who recognize the investment opportunity in oil and gas reserves and capitalize on it will profit handsomely.

There are essentially three ways in which you can *buy* and *own* oil and gas reserves in the ground. The first way is to buy common stock in those corporations that already own extensive reserves. Another way is to buy actual producing wells, and the reserves that go with them, through an investment in an oil income program. The third way is to buy ownership interests in public drilling programs that actually drill for new reserves. Each of them provides a way to capitalize on the boom in oil and gas, but it is up to the individual to determine which is personally suitable.

TAKING STOCK

In considering being a *stock*holder of reserves, there are two basic concerns. First, how do you choose which company or companies to invest in among the universe of corporations owning oil and gas reserves? Second, what are the pros and cons of this method of investing vis-a-vis the other two? As an investor in common stock, you have to be up on the capital gains tax treatment and how it affects your investment planning. If your major objective is to optimize your net *after-tax* return on your investment, then your strategy should be to go for a one-year holding period in order to realize long-term capital gains and have 60 percent of the gain excluded.

Choosing which oil and gas companies to invest in can be simplified by subscribing to an advisory service that follows the industry. You can also monitor the research reports and recommendations from top analysts who specialize in oil and gas and publish periodic reports distributed by brokerage firms.

On the other hand, if you would like to know which companies have the greatest reserves, a service out of Greenwich, Connecticut, publishes "Oil Industry Comparative Appraisals" in John S. Herold's *Petroleum Outlook*. It is an annual asset appraisal of petroleum companies—large and small, domestic and foreign—based upon their reserves, acreage, production, marketing, etc., plus other net assets.

One of the features of *Petroleum Outlook* is data on advances in asset values of the many oil and gas companies. According to Herold's research and analysis, only nine companies have been able to increase their asset bases at an annual rate in excess of 30 percent:

Houston Oil & Minerals (85%)
Mitchell Energy (37%)
Petro-Lewis (36%)
American Quasar (34%)
Texas Oil & Gas (33%)
Southland Royalty (32%)
Wiser Oil (32%)
Great Basins Petroleum (31%)
Pogo Producing (31%)

Among the major, fully integrated oil companies, the best annual rates of advancing asset values, according to Herold, have been achieved by:

Standard Oil Ohio (22%)
Marathon Oil (20%)
Sun Company (18%)
Union Oil California (18%)
Atlantic Richfield (15%)
Shell Oil (15%)

Canadian companies that have boosted their asset values at the greatest annual rate have been Voyager Petroleum (39%), Bow Valley Industries (30%), and Pan Canadian Petroleum (28%). Among the major Canadian

corporations, the best annual gains have been scored by Gulf Canada (18%), Shell Canada (17%) and Texaco Canada (15%).

By reviewing Herold's comparative data you can fairly easily identify which companies have the greatest reserves in North America, such as in Table 1. This list is the "class" of the industry, of course. But even in choosing among these giants, you may want to know which have been experiencing significant declines in oil and gas production, despite prominent price increases, as they will have difficulty in maintaining earnings growth. Standard Oil of Indiana, Mobil, and Texaco have experienced eroding domestic oil production.

You may also prefer companies that are diversified into other energy-related fields, such as uranium and coal reserves. The standouts in that respect are Atlantic Richfield, Gulf, Exxon, and Standard Oil of California. Each ranks among the top 20 companies that control *both* uranium and coal reserves. In addition, these same four concerns have been working on refining processes that will be very important elements in the future of nuclear energy.

Among the foregoing "Big Ten," Atlantic Richfield (ARCO) is in an especially good position. On the Alaskan North Slope and in the Gulf of Mexico, ARCO continues to develop new oil and gas reserves. This should assure it a position among a very few companies able to increase domestic production. In addition to its immense reserves of crude oil, natural gas, coal, and uranium, its acquisition of Anaconda last year gave it a big stake in gold, silver, and copper mining, as well.

Canadian oil companies tend to be a very attractive alternative to American oil companies because of the former's vast heavy oil reserves and relatively favorable taxation rate. Canadian companies already sell their production at world prices, in contrast to US companies, which are faced with another year or so of gradual decontrol before "old" domestic oil commands world prices. Also, Washington has just imposed a discriminatory excise tax on American oil companies for their so-called windfall profits.

A. G. Becker, Inc., which closely follows the Canadian oils, also provides us with appraised valuations of reserves. Becker's valuations of the Canadians tend to be substantially higher than Herold's "Oil Industry Comparative Appraisals" because the latter gives no value to heavy oil reserves until they actually enter production. Becker assumes that a very conservative 20 percent of the in-place reserves will be recoverable, thus compensating for overestimates of the reserves. Becker's appraisals of the "Canadian Eight" are provided in Table 2.

At 44 percent of appraised value, Dome Petroleum appears to be the current standout. Dome Pete has the largest acreage holdings in Canada (estimated to be 42 million acres) and is currently the sixth-largest producer there. Dome's overall working interests in current drilling activities make use of one-tenth of all the drilling rigs in Canada. In addition, it has a one-third interest in the primary acreage of the Beaufort Sea, which is considered to have great promise for major new oil fields. Moreover, Dome recently made several sizable acquisitions totaling $2 billion, including half-interest in the largest gas pipeline company in Canada.

Overall, a shareholder in reserves, in contrast to an investor in a public drilling program or an oil income program, has the single great advantage of *flexibility.* The ability to trade the common stocks of the oil and gas companies obviously is attractive to many investors who would not be comfortable with their capital committed long-term under someone else's control. On the other hand, the single great drawback to the common stockholder is the lack of tax advantages. Stockholders invest or trade with *after-tax* dollars and enjoy neither deductions nor sheltered income.

Table 1. "The Big Ten"

	N. American Oil Reserves (billion bbls.)	Appraised Value per Share	Stock Price 4/1/80	Stock Price to Appraised Value
Exxon	4.31	$140	$ 57	40%
Standard/Ohio	4.11	214	87	41
Atlantic Rich.	2.78	120	85 3/4	72
Texaco	2.20	113	33	29
Standard/Ind.	2.11	121	100 3/8	83
Standard/Calif.	1.73	140	65 1/2	47
Shell	1.68	84	59 1/4	70
Gulf	1.44	61	38 1/2	63
Getty	1.41	120	75	62
Mobil	1.31	173	66	38

Table 2. "The Canadian Eight"

	Appraised Value per Share (US$)	Stock Price ($US) 4/1/80	Stock Price to Appraised Value
Imperial Oil Ltd.	$109	$ 34 3/4	32%
Total Petroleum	57	21 5/8	38
Gulf of Canada	235	107	46
Dome Petroleum	123	53 1/2	44
Aquitaine Canada	86	39 1/4	46
Canada Southern Pete	46	12	26
Page Petroleum	42	17 1/2	42
Chieftain Development	52	24	46

PRODUCTION OWNER

Unlike owning shares in corporations that have reserves in the ground or investing in public drilling programs, there is a way for you to buy directly into actual reserves in the ground and enjoy tax-sheltered cash flow from your producing wells. There is no drilling for new oil involved, and there is no involvement in the stock market.

An oil income program gives you an opportunity to buy into *actual reserves and existing production* with an estimated commercially productive life of 12-15 years. The basis for profitability of investments in producing properties is predicated on the ability of the producing company, namely, the general

partner, to buy oil and gas reserves at a price that substantially discounts the future net revenue to be realized from the sale of production. The spread between the discounted purchase price and the ultimate dollar return represents profit to you, the investor.

There is nothing unique about buying and selling of oil and gas properties by discounting the future net revenues. It is the basis on which properties have been exchanged within the oil industry for decades. Companies that specialize in exploratory or developmental drilling are happy to sell their commercially productive properties, even at a large discount, in order to plow those proceeds into new exploration and development where the greatest profit opportunities lie.

The *real* risk of this oil production business becomes, not whether you'll get your money back, but whether the profitability of the producing properties will be as large as anticipated. By subjecting each proposed acquisition to a number of independent evaluations by geologists and petroleum engineers, a lesser degree of significant error may be achieved. Moreover, by diversifying each limited partnership into three or more separate acquisitions, the element of risk of overestimating the reserves they are buying for you is greatly diminished.

The difference between what they pay for oil and gas reserves discounted today and what they sell it for over the next 10 or 15 years is, of course, the margin of profit to the investors. Oil-producing companies sell their oil primarily to refineries and their gas to gas distribution companies on a contractual basis. This investment is currently generating a tax-favored cash flow of 12 percent *after* operating costs.

Direct investments of this nature in commercially productive wells are made through the medium of the limited partnership. There are several advantages of investing in limited partnerships that you do not enjoy with common stock. First of all, you share proportionately in the revenue and the costs, thus enjoying the tax breaks on depreciation, depletion, and interest expenses. Second is the advantage of direct ownership interests in specific properties. The avoidance of stock market risk is a third advantage of limited partnerships. A final advantage is that of limited liability. The major drawback of limited partnership interests is that they tend to be illiquid and non-negotiable.

Because of the start-up costs associated with getting each partnership going, there are tax deductions generated at the outset that are either passed on to the investors immediately or amortized over an intermediate time period. These deductions serve to reduce the taxes on the cash flow of a partnership in its early years. As the partnership continues its operations, it is entitled to realize cost depletion against the production of oil and gas that is sold, as well as depreciation on the well equipment. In addition, there are deductions for the interest expenses realized from utilizing leverage through bank loans.

Tax incentives significantly enhance the already attractive economics of oil and gas drilling.

The effect of these factors is that most of the cash flow from the investment distributed to the limited partners is nontaxable. The amount of cash flow that is sheltered will, of course, vary somewhat from partnership to partnership. In sum, an oil income program offers several key benefits to investors interested in direct ownership of reserves: low risk, significant appreciation potential, substantially tax-sheltered cash flow. Additional advantages are a modest first-year deduction, ease of reinvestment, and ease of liquidation once the partnership is fully invested.

GOING FOR NEW RESERVES

You can invest directly in ventures that drill for new oil and gas reserves onshore in the continental United States as a limited partner in a public drilling program. Investments of this type have been called tax shelters because they have built-in tax incentives designed to entice investment capital into this relatively high-risk area. Because of the high degree of risk associated with drilling for new reserves, these public drilling programs historically have been, and still are, restricted to investors in higher tax brackets.

The principal tax incentive for oil and gas drilling programs centers around initial deductibility, depletion allowance, and capital gains. Depending on the structure of individual programs, from 50 to 100 percent of your initial investment may be deductible in the calendar year of investment. In addition, the depletion allowance provides that about one-third of your future income from a drilling program will come to you tax free. The future redemption of a drilling program limited-partnership interest in most cases will be subject to preferential capital gains tax treatment. The combined effect of these three tax incentives is to significantly enhance the already attractive economics of oil and gas drilling.

There are risks in *all* oil drilling. The riskiest is, of course, the so-called wild-catting in pursuit of a significant new discovery in the remote frontiers of the planet. On the other end of the risk continuum is the safest form of drilling, known as box score development, or secondary oil recovery. That means drilling in areas of widespread oil and gas deposits, resulting in a very high percentage of wells being completed but also known to result in marginal economic return.

Between these two extremes fall most of the oil and gas drilling program activities conducted by public drilling companies. There are three basic types of drilling: *exploratory, developmental,* and *balanced,* or combination, drilling.

Exploratory drilling is conducted in new areas that are believed to have a very high probability of containing hydrocarbons. Nevertheless, the industry average of commercially productive wells to dry holes is one in nine. Developmental drilling is conducted in areas proximate to existing production. The industry average is that, for every four wells drilled in an existing field, three will become commercially productive. The trade-off for the public drilling companies is the lower cost for acreage and royalties on new exploratory properties and greater potential payout versus much higher costs to drill developmental wells.

The risk-reward ratio is probably an unwritten law of economics. Risks are commensurate with the rewards. High risk, high reward; and vice versa. So it is in oil drilling. The really *exploratory* drilling programs will give you the maximum tax deductions and, if successful, the greatest potential payoff. If unsuccessful, however, they also have the greatest probability of loss of

(*Continued on p. 58.*)

Space Settlers: An Endangered Species

An international regime declares the Moon, asteroids and planets off limits to space settlers?

The plot of a science-fiction movie?

No, it would be the consequence of a U.N. treaty the U.S. could sign any time.

The "Moon Treaty," as the New York **Times** calls it, would:

- —effectively impose an indefinite moratorium on the commercial (free world) development of nonterrestrial resources.
- —impose an OPEC-like Earth controlled regime on the Moon and all other celestial bodies
- —effectively prohibit individuals from owning real property
- —prohibit individuals in space from obtaining political asylum or changing nationality
- —open vehicles, installations and habitats to search by any Earth government of the international space regime

If it weren't for the efforts of **Reason** (see Robert Poole's editorial in the December '79 issue) and the L-5 Society, this treaty would have already been signed into law, and the endless frontier would have been closed before it was opened.

Please join with us today in this historic battle to preserve our right to pioneer space. Donors of: $5.00 or more will receive a copy of the treaty and four pages of comment; $20.00 and up will receive the above plus sixteen pages of analysis; $50.00 and up will receive the above plus a year subscription to the **L-5 News** (regularly $20.00).

"We don't have to worry about those folks getting loose."

L-5 Society
1620 N. Park
Tucson, AZ 85719

YES! I want to ensure individual freedom and opportunity for everyone in space. To help shape our future, enclosed is my donation of
☐ $5 ☐ $10 ☐ $20 ☐ $50

Mr/Ms _____

Address _____

City _____ State _____ Zip _____

Please make out your check to the L-5 Society, Moon Treaty Fight. Contributions are tax-deductible within the framework of the law.

"A call for the next step—the positive reconstruction of our local governments through free market alternatives."

— William E. Simon, former Secretary of the Treasury

CUTTING BACK CITY HALL

by Robert W. Poole, Jr.

Foreword by William E. Simon

Local governments can *prosper*, even with the growing tax revolt, says Robert Poole, and better services can be provided at lower cost. CUTTING BACK CITY HALL is the first comprehensive discussion of how communities across the country are coping with reduced revenues. Poole cites case after case, with specifics and cost figures, to show how and where private contracting, user fees, and modern management techniques are already bringing efficiency and cost reduction to public services. He then suggests specific ways in which legislators, citizens, and administrators can go about cutting back city hall. And he provides the names of leading companies (including consultants) that offer services to local governments on a contractual basis, and an extensive bibliography of relevant reports, studies, and publications.

Robert Poole is Chairman of the Local Government Center, and Editor of *Reason Magazine*.

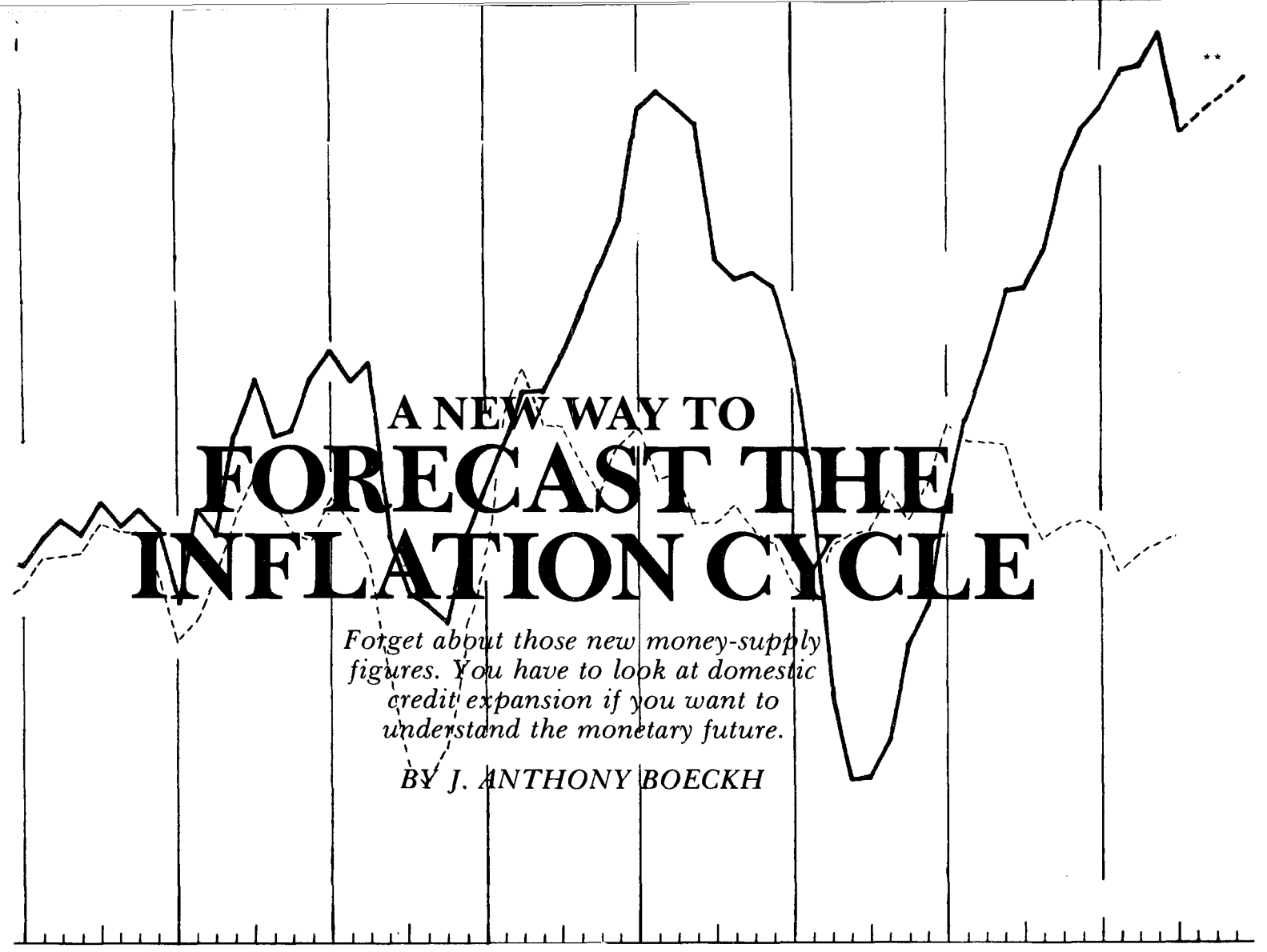
UNIVERSE BOOKS
381 Park Ave. So., N.Y., N.Y. 10016

Please send me ____ copies of CUTTING BACK CITY HALL at $12.50 each, plus 10 % postage and handling.
My check/money order is enclosed for $_____

Name _____

Address _____

City _____ State _____ Zip Code _____



A NEW WAY TO FORECAST THE INFLATION CYCLE

Forget about those new money-supply figures. You have to look at domestic credit expansion if you want to understand the monetary future.

BY J. ANTHONY BOECKH

Inflation is a form of national bankruptcy. It is not only a symptom of deep political and economic malaise in society but causes its own disastrous consequences for society that are well known. What is so striking about our contemporary inflation is how politicians, bureaucrats, and the public have become resigned to it, as though it is a disease beyond anyone's control. The typical line one hears from government, which ultimately must take responsibility for inflation, is that "we too are victims of inflation."

While one can argue about the ultimate causes of inflation—whether it be lack of a gold standard or fixed exchange rates, budget deficits, the expanding welfare state, declining productivity, environmental restrictions and government controls, etc.—one thing is certain: inflation cannot exist and flourish without central bank cooperation, accommodation, and even encouragement. *Inflation must be financed.* If central banks are going to finance it, they should do it in the open so that everyone knows what the rules of the game are. One of the great problems with inflation is that central banks and governments say they are not going to permit inflation, that they are going to pursue anti-inflationary monetary policies, and yet they do precisely the opposite. My purpose here is to explain why this has been the case in the United States. The story is the same in Britain and Canada, where inflation has been a similar problem.

In addition to looking at how inflation is financed, I will show how it can be measured in a way that gives a clear guide to policymakers if they really want to stop inflation. The analysis gives a clear guide to investors and people in business, as well, because it indicates when and how government policy and interest rates must eventually respond to accelerating inflationary pressure. The analysis is useful in explaining what has happened in the past and provides a useful technique for forecasting, an example of which is included with some conclusions based on data available at the end of February 1980. The reader, who will be seeing this well after it was written, should keep in mind the speculative nature of the forecasts, since at the time of writing events were moving dramatically, and in an election year some equally dramatic political response was to be expected.

MONETARISM RUN AMOK

The progressive shift away from the simplistic demand-management and fine-tuning policies of the 1950s and '60s to so-called practical monetarism, beginning with Arthur Burns at the Federal Reserve in 1970, was supposed to be a watershed in official economic policy. The belated discovery of "money" at the Fed 10 years ago and the

supposed containment of money supply growth with predetermined target ranges set by the Fed held out great hope that the economy could be returned to a noninflationary stable growth path.

In remarkable contrast to the hope generated by this policy shift, however, we have experienced two runaway inflations. The first, which reached its full flowering in 1973-74, saw the increase in wholesale prices hit a peak of 32 percent. The current accelerating inflation was still raging out of control at the end of February, with the rate of increase of wholesale prices hitting almost 20 percent.

The obvious question is, What went so badly wrong with "practical monetarism"? Assuming that intelligent, well-meaning people run the Fed, why has the actual performance of the economy and inflation been so disastrous? The reason is that the monetary authorities do not know what they are doing. By focusing on a relatively narrow measure of money, such as *M2*—or, even worse, *M1*—they are missing the actual financing of excessive credit demands. They have, in effect, permitted or acquiesced in a massive credit inflation. Even apart from definitional and measurement problems with what money is, they have focused unduly on the supply of and demand for money, removing themselves from the far more significant process of credit creation and how money comes into existence.

Money comes into existence in a roundabout way because people, firms, governments, and so on demand credit to finance expenditures. When these demands are excessive relative to the supply of domestic savings and the central bank is attempting to hold interest rates down, the result is excess demand, where demand runs way ahead of the domestic economy's ability to supply. A broad measure of money provides one useful barometer of such potentially inflationary pressures. There are circumstances, however, when even such a measure can prove extremely misleading. A more accurate and comprehensive guide is, in fact, provided by the underlying excess credit creation that finances these excess demands and provides the motive force behind the inflationary process.

In assessing whether inflationary credit demands exist in an economy, it is essential to utilize a framework that takes into account broader monetary and credit aggregates rather than conventionally published Federal Reserve money data. Only then can one get an accurate barometric reading of the magnitude of money and credit excesses. So long as the authorities choose to focus on a defective inflationary barometer for guidance, they will stumble from one crisis to the next, leaving intact the long-term secular rise in inflation and interest rates.

CREDIT PRESSURE

Domestic credit expansion (DCE) is an elusive concept. Just as money supply has a habit of changing form at the very moment when everyone thinks he knows what it is, so DCE can be defined in a number of different ways.

By focusing on money supply and demand, the Fed has removed itself from the far more significant process of credit creation.

To make sense of any of the myriad financial statistics spewed out by the official reporting agencies, it is crucially important to have some conceptual framework within which such information plays a vital role. And the objective here is to provide a framework for interpreting the data available, not necessarily—nor, as it turns out, usually—the information spoonfed by the authorities to their waiting and expectant public. Development and use of DCE in the United States (See "DCE: An Indicator of Excess Money Creation," *Bank Credit Analyst,* May 1978, p. 29) is a piece of the complex and half-completed jigsaw that can be used to provide insights into the evolution of market behavior.

Low growth of the money supply (even when broadly defined) does not necessarily mean that excess demand is also low—it would be nice if that were so. It could be that instead of excessive demand (financed through the creation of new credit from the banking system) showing up in higher prices, the money is spent on imported goods and services and consequently flows abroad. As with rising prices, the deterioration on external account must sooner or later lead to tighter monetary policy and higher interest rates. Moreover, the effect will still be inflationary, but the lags will take longer to work out—exactly the process we are seeing in the United States at present.

Attempts to improve the balance of payments directly, or depreciation of the exchange rate (nature's own cure), will turn the excess demand into inflation of the domestic price level. But the cause is still the original creation of excess demand. It is essential not to lose sight of this in all the confusion as the traditional whipping boys are dragged out for their customary ritualistic flogging. For example, President Carter continues to blame the current high rates of US inflation on OPEC for raising the price of oil and on Congress for not passing his energy bill. Yet Switzerland and Germany pay OPEC prices for *all* of their oil and do not have legislative problems with energy bills, yet they have far lower inflation rates than the United States does.

DCE is an attempt to identify this underlying excess demand, financed originally through excessive credit expansion. In this sense it is like the supply of money but abstracts from the leakages abroad. But it also has an added advantage, which takes on growing importance at this time of continuing financial innovation: it takes into account the potential credit-creating ability of the banks that is financed through sources other than those included in definitions of deposits subject to Fed control. The difference in the growth rates of DCE and the money supply are truly dramatic, as discussed below.

The measure of DCE employed here is, in fact, different from that found in official statistics, such as those of the International Monetary Fund and Bank of England. That need not cause any concern. Like the money supply, DCE can come in many different shapes and sizes. The measure explained here has been constructed to reflect the borrowing needs of the total nonbank domestic economy—government at all levels and the private sector—that have not been financed by loans from fellow citizens.

In the economy as a whole, the public and private sectors combined have a borrowing requirement that must be financed. It can be financed in three

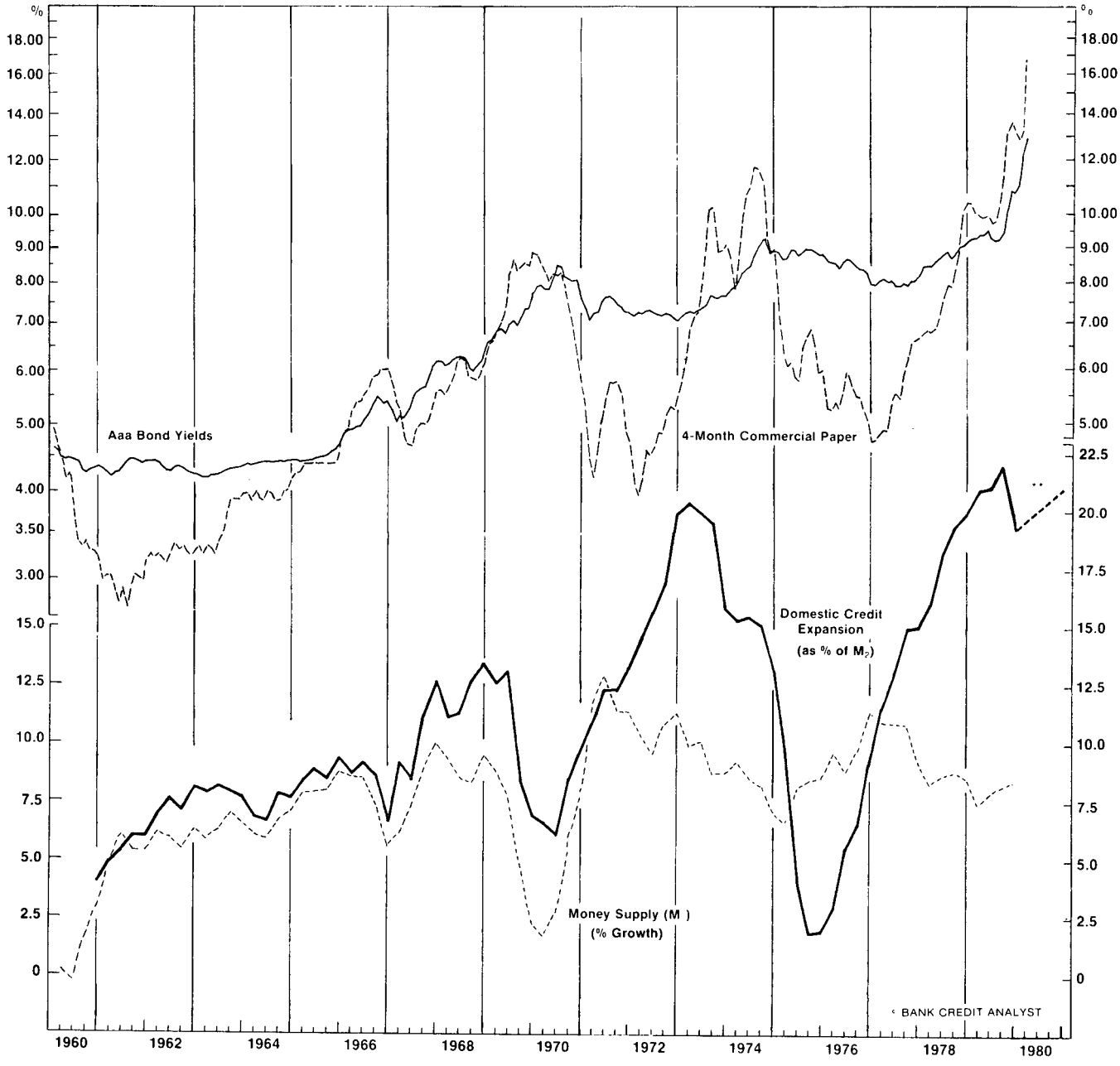
ways: from the nonbank domestic sector, from foreigners, and from the domestic banks. When borrowing requirements are excessive relative to domestic savings, additional credit can be created through the banking system or from abroad. This new credit is available to finance additional expenditures and is potentially inflationary; how inflationary depends on the current stage of the business cycle. The DCE series is employed in an attempt to identify the underlying demand pressure in the economy before all the camouflage of currency outflows and deposit distortions has been added.

The chart below plots quarterly DCE figures for the United States since 1960. It is shown as a four-quarter moving total expressed as a percentage change on the money stock (*M2*) of the previous year. Also shown is the rate of growth of *M2*. Each of the four cycles can clearly be seen. There is a progressive acceleration of growth in DCE above *M2* growth during the expansionary phase of each cycle when interest rates are rising, followed by a contractionary phase when DCE falls relative to *M2*.

Three points emerge from the analysis of DCE relative to *M2*:

1. Each cyclical rise of DCE is larger relative to *M2* than the previous cycle. In particular, during two cycles since 1970 following the Fed's move to a monetarist policy of supposedly controlling money supply, the amplitude

DOMESTIC CREDIT EXPANSION, MONEY STOCK, AND INTEREST RATES



*D.C.E. MEASURES BANK AND OVERSEAS FINANCING OF THE PUBLIC AND PRIVATE SECTORS.SEE TEXT FOR FULLER EXPLANATION OF DEFINITION AND CALCULATIONS.

**THE FIGURE FOR 1980 IS AN ESTIMATE MADE BEFORE THE CARTER PACKAGE OF MARCH 14TH. IT WAS DESIGNED TO SHOW WHY A PACKAGE WAS NEEDED. SEE TEXT FOR EXPLANATION OF THE FORECAST AND HOW IT IS USED.

of the cyclical swings has become far greater.

2. From the point of view of monetary control, it is extremely misleading to focus on *M*2. During the last three cycles, *M*2 decelerated well before the end of the expansionary phase of the cycle, while DCE was still accelerating. Focus on *M*2 creates a tendency for the authorities to relax policy too early, allowing inflationary momentum and speculation to gather enormous momentum at the end of the boom and thus forcing the central bank into overkill. This helps to explain why each cycle has become more extreme and more dangerous.

It should also be noted that the narrower definition of money—*M*1 and its current variants, *M*1A and *M*1B—are far smaller relative to DCE than is *M*2. Moreover, with a structurally high level of interest rates, the opportunity cost of holding liquidity in non-interest-bearing form becomes enormous. Hence, concentrating attention on *M*1 can be even more seriously misleading than using *M*2. An excellent example of this occurred in late 1978 and early 1979. *M*1 decelerated sharply, creating widespread fears of recession on the part of the naive monetarist school. The Fed authorities eased up and created a huge extension to their inflationary monster. They made the same mistake in late 1973 and early 1974 and also in late 1968.

3. From a timing point of view, it is evident that DCE leads the interest rate cycle. At the trough of the cycle, DCE growth is faster than *M* growth. But it takes some time before interest rates turn up. At the top of the cycle, DCE growth peaks out well before the peak in rates. In fact, around the last three cyclical peaks—1966-67, 1969-70, and 1974—short rates did not peak out until DCE had fallen sharply and for four quarters. Since DCE in the current cycle made a new high in the third quarter of 1979 and fell only moderately in the fourth quarter, with the likelihood of another rise in the first quarter of 1980, it would seem that interest rates might be some way from a peak in the absence of a change in either monetary or fiscal policy.

DCE IN YOUR FUTURE

DCE makes the past understandable, explaining where the economy has been and why certain things have happened. For example, it explains very well the magnitude of the rise in US interest rates in 1973-74 and from 1976 to the present. It also explains the chronic weakness of the US dollar, particularly during expansionary periods of the cycle.

To get some idea of what could happen in the period ahead, it is necessary to attempt some forward estimates of DCE (see table). This is done by estimating the federal government's borrowing requirement and the proportion of it that will be absorbed by the nonbank domestic sector. The overall federal borrowing requirement figure is the sum of the government's own required borrowing needs plus agency borrowing and mortgage pool securities guaranteed by government agencies, all exclusive of acquisitions by government agencies and the Federal Reserve. This gives the federal government contribution to DCE. Added to that is estimated bank and overseas lending to other levels of government and to the private sector. Because the bank-related commercial paper market and money market funds have become so important as quasi-banking institutions, they are included as well. Subtracted from the total is bank lending to foreign branches, as this does not add to domestic credit creation.

Estimates for the major components are made as an example of how the forecaster can use DCE in order to assess trends in US inflation, interest rates, and the dollar and thus be in a position to assess how and when government policy might be forced to change. These estimates are necessarily tentative and dependent on actual and anticipated government policy at this time. As policy changes, so these forecasts should be updated. Moreover, in the light of these projections we would very much hope that policy would be changed.

The estimated total government borrowing requirement is $95 billion. The projections include the very conservative assumption, as a result of the high level of nominal interest rates, that this can be absorbed completely by the nonbank sector. Thus the federal government's direct contribution to DCE could be close to zero. This is not by any means intended to suggest, however, that the government's borrowing requirement is irrelevant. On the contrary, a figure of about $100 billion, or 6½ percent of GNP, is hardly appropriate in a year of runaway inflation, overheated economic activity and labor markets, and interest rates at the highest level in US history. In effect, the federal government, by requiring so much financing, is and will be preempting credit flows to the private sector. As a result, the private sector is forced to finance heavily at the banks and from foreigners. To the extent the private sector is forced, permitted, or encouraged to finance at the banks, money supply rises. Since the government borrowing requirement is projected to be very high in 1980, bank and overseas lending is estimated to grow at a 15 percent rate, down somewhat from 1979, with commercial paper issued by banks and money market funds to contribute another $38 billion. As a result, DCE is projected, on unchanged policies, to

DCE PROJECTION

	Projected 1980 (billions)	Actual 1979 (billions)
Federal government borrowing requirement	$ 95	$ 69
Less: Absorption by nonbank domestic sector	95	82
Federal contribution to DCE	0	−13
Plus: Bank and overseas lending to private sector and junior governments	160	124
Commercial paper issued by banks	28	44
Money market funds (net of CDs and bank-related commercial paper holdings)	10	20
Less: Lending to foreign branches	nil	7
Domestic credit expansion	$198	$168

grow by almost $200 billion in 1980 compared with $168 billion in 1979. As a percentage of *M2*, DCE growth would amount to almost 21 percent.

DCE is, as discussed above, a monetary concept, but it is much broader in scope than the simple monetarist notion of trying to control a monetary aggregate that is a rather narrow part of the economy. It includes the effect of the balance of payments on the financial system and money growth. It focuses on the creation of credit, which is the starting point for countries heading into serious financial disorder; and it gives an early-warning signal of when and how policy should change. Governments that ignore excessive DCE do so at great risk. The US government throughout the 1970-75 cycle and again throughout this cycle ignored the warning signs of excessive credit creation, current account deficits, chronic dollar weakness, devaluations, and a huge build-up of dollars in foreign official institutions. As a result, it encouraged massive speculation in inflation hedges and accelerating price inflation, which by early 1980 was into the runaway range of 17-19 percent.

While the DCE projection of almost $200 billion, or a 21 percent increase compared with the money stock, represents some leveling off, it is still wildly excessive and suggests a continuing accommodation to very high rates of inflation. In this environment, with intense military and geopolitical tensions in the world and a major rearmament program under way, stability is not likely to be restored. In fact, instability could be further heightened and the continuing crisis deepened.

GOVERNMENT OPTIONS

Having created such a massive and frightening speculative bubble, runaway inflation, and a bond market collapse, the government's options are relatively few. By focusing on DCE, one can narrow down the basic options in order to get some idea of what the government will do.

1. *Nothing.* This has been the "game plan" of the past three years. Essentially, it has been a bet that the boom would blow itself out at a relatively modest rate of price inflation. It has not worked because the Fed has continued to accommodate the boom with accelerating DCE and persistent efforts to protect the housing industry from rising interest rates. It could be that the game plan will be brought onside by a recession already triggered, but it remains a dangerous gamble.

2. *Reduce the federal government borrowing requirement by:*

- Cutting government expenditures. In practice, this is a hopeless task in the short run for almost any government. For a populist US government in an election year it can safely be ignored.
- Raising taxes. For the same reason as above, this can also be ignored.
- Reducing federal assistance to housing. Since housing is as sacred politically as motherhood, and because the industry is already in an advanced state of collapse, this option can effectively be ruled out as well. Some cosmetic moves in the area of restraint for fiscal 1981 can probably be expected, though.

The performance of the economy and inflation has been disastrous because the monetary authorities do not know what they are doing.

3. *Impose orthodox monetary restraint.* Because the growth in bank credit is so wildly excessive, it might require interest rates substantially in excess of 20 percent for a while to break the bubble. Should interest rates go to such levels, widespread bankruptcies could be expected in thrift institutions and weak corporations. Hence, any dramatic move in this direction before the election is unlikely, but one should expect more cosmetic moves in this area.

4. *Controls.* By a process of elimination, one comes back to the controls option as the refuge of desperate governments that do not know how to deal with a crisis they have created. Until the Thatcher government, this was always the path followed in Britain—inflate; and when chaos strikes, go for controls. Once the United States was past the point of no return after 1978, the government locked itself into a situation in which controls became virtually inevitable given the attitude that painful economic correction must be avoided. Toward the end of February, not surprisingly, the trial balloon of the controls option was floated in a number of quarters, and it is highly probable that they will eventually be imposed. Their timing will depend on when the "crisis" becomes politically intolerable. There are two major types of controls that the US government could go for—wage and price controls and credit controls.

In short, the United States is faced with a true domestic crisis. Price inflation is still accelerating and the bond markets have ceased to function. Unless the economy suddenly turns down swiftly enough to break the inflationary momentum and credit demands, the authorities cannot for long maintain a policy of benign neglect. Since fiscal deflation is effectively out of the question, the authorities have no choice but further monetary tightening or the imposition of controls.

PRIVATE SECTOR SQUEEZE

The essential problem is that for several years excessive and clashing credit demands in the economy have been allowed to generate excess credit creation, excess money growth, and rampant inflation. The consequences of this in terms of massive speculation, collapsed bond prices, collapsing housing, and a sharply deteriorating position of thrift institutions means that the authorities will have to intervene whether they like it or not. If the public sector does not reduce its claims on the economy for credit and real resources, then the private sector must be forced to do the adjusting. The problem is that the current level of interest rates appears to be nowhere near high enough to squeeze out the private sector.

The essential rationale for controls is to squeeze out the private sector at a lower level of interest rates than would otherwise be the case. While one can debate the various effects of different types of controls, investors and businessmen must not lose sight of the real point of the exercise—to squeeze the private sector. Thus, an effective controls package must be painful, just as an effective credit squeeze through orthodox monetary restraint would be. The longer such policies are delayed, the more devastating will be their consequences.

Borrowers are going to be denied credit at some point, either by fiat or by interest-rate rationing or both. Since the corporate sector's financial

deficit will be widening from its already enormous level, as the economy slows further and costs continue to escalate, a painful squeeze must lie ahead. It is difficult to see any way out of the bind that the corporate sector will be in. The strain will remain until a decisive economic downturn is created, inventory liquidation is triggered, and ultimately reliquification at a lower level of inflation and interest rates.

Wage and price controls represent a further risk to the corporate sector because in an election year following two years of lagging real incomes, unions will only buy the package if they clearly can see some gain to themselves. Therefore, one must be prepared for a controls program that allows wages to rise relative to prices. Thus, a further risk to the corporate sector's financial position exists on this score.

In effect, the real cutting edge in a private sector squeeze is to force a widening of the corporate sector financial deficit and hence cause an increase in its external borrowing requirements, while simultaneously reducing its access to credit. A combination of effective credit controls and wage/price controls, favoring the former, is a potent weapon in accomplishing this end.

The bond market collapse of 1980 is creating its own conditions for reversal since the government cannot allow it to go on indefinitely. As for wage and price controls, the bond market would probably react favorably to them in the short run because of its deeply oversold condition. Beyond the short run, the bond market reaction would depend on the effect controls would have on actual economic activity, inflation, and credit demands.

With regard to the economy, it is also very difficult to assess how deflationary controls would be. Credit controls would, *if effective,* clearly reduce demand. If wage and price controls favored wages, then overall demand might rise as the personal sector would probably be stimulated more than the corporate sector deflated. But if tough restrictions on bank lending were imposed, the increase in the corporate sector's deficit could not be financed and hence unemployment might rise rapidly as firms dumped labor and inventories and cut back on capital spending.

The point is that runaway inflation creates great risk, volatility, and instability. Ultimately it forces the government to act, and this adds to instability because one cannot know the timing of the intervention nor whether it will have the effects desired or whether the effect will be perverse. Moreover, the short-run effects are often in the opposite direction to the longer-run effects. For example, after President Nixon's August 15, 1971, package of controls, floating of the dollar, import surcharges, etc., the stock market rose for a few weeks and then fell sharply. Should we get another package, it could well involve a combination of many moves that might have conflicting effects.

Investors and businessmen must not lose sight of the real point of controls—to squeeze the private sector.

DCE is an extremely important monetary concept. If the authorities were serious about containing and actually reducing inflation, they would monitor it and change either or both monetary and fiscal policy when it first becomes excessive. This would avoid the situation they are in now and were in in 1974: having to change policy too late. By reacting very late, they allow inflation to build up tremendous momentum, which ultimately forces them into extremely unpleasant policy changes that risk serious overkill. Politically, when the risk of overkill appears high, they are very likely to resort to controls of one or more types—wage and price, credit and foreign exchange, depending on where the symptoms of instability are most extreme. The imposition of controls does not necessarily mean that the ultimate economic correction won't be severe. Moreover, it leads to massive distortions that further complicate the distortions from inflation; they squeeze the private sector, whose health is required to supply the goods and services to ultimately bring prices down. Finally, the removal of controls sparks a major catch-up or free-for-all that creates a whole new set of problems, which in turn increases the odds of a new set of controls. It is thus that a country can slide down the slippery path of socialism ultimately to authoritarianism.

DCE is also a useful concept and indicator for businessmen and investors because it clearly points out where a country is heading with regard to inflation, balance-of-payments problems, and interest rate trends. It also provides a highly useful framework for analyzing government policy changes.

Postscript: On March 14, several weeks after this article was written, the president and the Federal Reserve Board announced a new anti-inflation package. The major point was to reduce bank credit expansion—an encouraging acknowledgment of its importance. It was unfortunate, however, that so much emphasis was placed on credit controls, since they will add to distortions in credit markets and, if maintained, create even greater problems for the future. It was also unfortunate that no serious effort was made to contract the public sector's claims on real and financial resources. Thus, as expected, the private sector once again will bear the brunt of retrenchment, adding to long-run inflationary pressures.

It appears at present that the monetary authorities are serious about credit restraint. If so, the inflationary bubble will burst and a serious recession will develop. The big question then is, Will there be another major reflationary effort, to be followed by another boom-bust cycle, leaving intact a very long-run trend of accelerating inflation? One cannot help but suspect that, should the economy fall apart and unemployment rise sharply, the battle against inflation will cease and all efforts will be turned to manning the reflationary pumps. Clearly, investors and businessmen should continue to track DCE. It will once again provide a good lead to the extent of effective credit inflation and renewed pressures on the US balance of payments, the dollar, inflation, and interest rates.

J. Anthony Boeckh has been the editor of Bank Credit Analyst *for 12 years and is a director of the Free World Fund, a mutual fund specializing in international investments.*

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Make the IRS Your Partner

How the average person can use real estate to shelter his income from taxes.

BY ROBERT HAISMAN

Every year around April 15 you hear complaints that "few rich people pay any tax," that "the tax burden in the United States is carried by the beleaguered middle class." And a common assumption is that the people who get away with paying little or no tax are doing something fraudulent, or at least questionable under the often-ambiguous tax laws. But doesn't it make sense that, since they are so spotlighted in the public eye, the IRS would scrutinize their tax returns a whole lot quicker and in greater detail than yours or mine? In fact, their paperwork is in much better shape than 90 percent of taxpayer submissions.

Well, if they're not cheating, what's the super secret of paying practically nothing, while so many of us wind up with a sizable "contribution" every year? The biggest secret is that there *is no super secret.* You and I can enjoy the very same advantages. The games the big boys play are open to all of us—but it does require getting into position to be able, like them, to deduct those investment tax credits, depreciation, and a whole host of associated write-offs. And you do it by making the IRS your partner, by holding on to the earnings that are now going to pay your income tax and using them instead to increase your own personal fortune.

The sound business practice involved here is to leverage your equity position through maximum borrowing, which carries an element of risk. Depending upon when you were born, or just how much "remember the depression" philosophy your parents may have showered upon you, this could cut across your grain of thinking. But to get an economic leg up on inflation, you *must* become a part of our free-enterprise system. To accomplish this feat, to join the group, you will need to pay for your ticket on the way in. There are only three legitimate ways to acquire these means: earn and accumulate it (the depression-era legacy), inherit it (the lucky way), or borrow it (and that's what we're talking about here).

A PENNY SAVED

Never having had much and consequently being very naive in financial matters, most of us have approached money on an ultraconservative basis—like saving money in the bank. If government regulation were consistent, banks, like the cigarette companies, would have to print on your statement, "Banking is dangerous to your financial health," as the five to eight percent you think you are making is really "bottom lining" at a considerable *loss* because of inflation. A lot of us consider our home our prime investment and inflation hedger, and that's a good basic choice.

The problem here is that we also dream about the day we'll have the mortgage paid off, and that's not too smart. If that's your plan, you're overlooking a big chance to get ahead and stay there by leveraging your equity into a free-enterprise venture. Such a venture doesn't have to be a change in your career or a brand-new business; it can be something you are already familiar with. Let's take a typical "oh so true" example and see what we can do with it. How many people do you know like...?

Stanley White is 49 years old, married, two kids, one of them still in college. The Whites bought a tract house in the early '50s for $10,000, with $1,000 down—$500 of which they borrowed from his folks—on a 25-year loan. They've lived there ever since and are quite proud of the fact the mortgage was paid off two years ago. On today's market, the house is worth $60,000+ (would you believe it?). Stanley also has $14,000 of savings in the bank, another $8,000 in company stock (which is about 20 percent less than the average price he paid for it), a $10,000 life insurance policy with a cash value of $6,000, a fairly new car valued at about $5,000, and $1,000 vested interest in the company's new retirement plan. Sound pretty good?

Stanley's salary is now $28,000 a year—quite a ways up from the $4,800 he started with 25 years ago. The Whites live in a state that doesn't have an income tax; their federal tax base is 25 percent, taken out of the paycheck in advance ($7,000, not counting So-

Illustration by Rick Seward

cial Security). Through the years they have learned to live quite modestly and are comfortable and happy with the way they have managed things. Everything here seems okay...on the surface.

Stanley will work 16 more years until he's 65. Let's give the Whites the benefit of the doubt and say that they can save $2,000 a year, even with today's soaring prices. This should give them over $50,000 in the bank by that time, but with meager bank rates and his 25 percent tax on the interest, plus inflation and the consequent loss, they will have a buying power—even with a conservative 4.5 percent inflation rate—of less than $25,000. Conversely, the Whites' home will ride with inflation, maybe be worth $90,000 or more. But can they afford to sell it? Wouldn't the cost of replacement be equal to what they sold?

Contrary to the naive belief that when we retire we're all ready to change our lifestyles and slink off to a cave on Social Security, Stanley will want to vacation and do all the things he has yearned for but never had the time to do. Won't this require even a bigger monthly budget? Where's it going to come from? The Whites will dissipate their savings very quickly just supplementing Social Security income. They're in a box and not even aware of it.

BORROWING POWER

There doesn't have to be a sad end to this story, because Stanley has *equity*. True, it's not doing him any good, but if he leveraged it, it could do him a whole lot of good. First off, we mortgage his house at as much leverage as we can get, probably 80 percent of market value, giving Stanley $48,000 in cash and...what's that?—"a mortgage payment of $_____ per month that he didn't have before"? True, but just wait. Next, we borrow the cash value on his life insurance policy ($6,000). Why? Because we would borrow even if we didn't need the money, as an after-the-fact attempt to partially retrieve a very poor investment.*

So now, between the house and the insurance, we've gathered up $54,000 worth of leverage for old Stanley. We'll leave his stocks and retirement fund alone—we don't need it, and every man is entitled to his dreams, even if they don't materialize. We will take, however, $11,000 of the $14,000 in the bank, leaving $3,000 for emergencies or to start a Keough (tax-deferred) retirement plan under Mrs. White's name. This gives us $65,000 of hard-cash leverage to work with. We use it as cash down payment, leveraged at 75 percent, on a good commercial building or an apartment building or a combination of duplexes and triplexes or four more residential houses. Now our Stanley is the proud owner of combined real estate valued at $320,000, a real honest-to-goodness American entrepreneur. To see how all this looks on a "before and after" net worth statement, see Example A.

We won't really expect our new acquisitions to produce a net addition to income. We just want them to pay for themselves—discharge their debt, taxes, insurance, etc. But what about Stanley's new payments on his own home? If he isn't earning anything on the new investment, where does he get the money to make those payments? Why, from his partner, the IRS—with some of the $7,000 he *was* paying in income taxes. "Uncle" is now helping him to become his own man within the free-enterprise system.

Here's how it works. Remember that we've assumed that Stanley collects rents from his new business prop-

* An insurance policy buys *only* one thing—an estate, if you die too soon. Any bill of goods you've been sold that *overpayment* of premium (whenever there is cash value) constitutes a decent return on investment is pure "horse pucky" out of the depression years. But once you've made the mistake, you can salvage something by "arbitrage." Since the insurance company pays you about 3 percent on your overpayment, they are more than happy to let you borrow your own money back at 6 percent. You, in turn, can certainly place this money today at 8 to 10 percent interest, making several percentage points on the deal (arbitrage). Could you have circumvented the middle man in the first place? Sure; you could have bought the cheapest *term* insurance policy you could lay your hands on.

erty that just cover his interest on the $195,000 loan, as well as taxes, insurance, maintenance costs, and so on. So for income tax purposes, his new business income will be offset by his new "out-of-pocket" business expenses. But he will also have the decided advantage of being able to depreciate his newly acquired business property—that is, to claim the depreciation as an expense. This, in turn, will mean that the business will now show a loss (but remember, there's no added cash outlay involved), and this loss will be used to offset taxable income from Stanley's job.

For example, say the property we've bought for $260,000 has improvements worth $170,000. The land, which accounts for the other $90,000, cannot be depreciated because it's always there, does not deteriorate like a structure, and, in fact, is the one thing that increases the overall value of your investment, especially during times of inflation. The $170,000 building can be depreciated on an established schedule, using the "straight-line method," at $8,500 per year for 20 years, or the period can even be shortened to 15 years, at $11,333 per year, if he needs more protection. Other methods available—"double declining balance" or "sum of the digits"—would allow for depreciating a whole bunch now and then less downstream, instead of the same amount each year.

This means that Stanley shows a loss of at least $8,500 on his business Schedule C (of his federal income tax form). When this is transferred to the appropriate line on his 1040 submission, it will serve to reduce his overall taxable income accordingly. In addition, there is a 10 percent investment tax credit that he may use (one time only) in any given year. Plus, with the mortgage on his own home, he now has interest payments to add to his itemized personal deductions.

So you can see how advantageous is depreciation as a tax avoidance vehicle. This is why an individual who has owned a piece of property over a long period of time, and has depreciated it to or close to a "book value" of zero, may well elect to exchange it for another property of similar value, just to start this depreciation process all over again and, by exchanging, to defer taxes on the capital gain.

Sixteen years from now, Stanley's home might be worth over $90,000, and if we believe that (and we should), his combined real estate will be worth over *a half-million* and will be two-thirds paid for. And it all happened without changing his lifestyle one bit!

TAX-AWARE INVESTING

Elizabeth (Betty) Bentley was and is a liberated woman. She set out quite early in life to provide for herself, so she purchased a home and has made investments in land from time to time. She has owned and managed a very prosperous antique and gift business for the past 20 years and would like to expand it, but despite all honest effort with personal and business deductions, she cannot get her net income below $24,000 and a 40 percent bracket. "If I make more money, my income taxes will go up even further, and I just can't see working for nothing."

The problem here is that Betty's investments, though admirable, were the wrong kind for her. The land buy is unimproved and offers no (much-needed) advantages of depreciation. Her "deferred tax" land partnership is self-contained, most of its profits eaten up by administrative costs over which she has no control, and it does not afford tax relief *now* when she needs it. Obviously, we need to get rid of the land, the land partnership, and her house for that matter—she only bought that big place for the tax and interest write-offs.

But if we sell, Betty will be exposed to a large capital gain because she bought the house and land some time ago and has a large potential profit in both. So what we're going to do is use the equity in this property for a leveraged trade upward, like a big apartment complex, and defer all such taxation until she dies, or "forever," as Betty likes to put it. The land partnership lacks liquidity, and even though they say it's worth $60,000, we'll have to discount it to $50,000 (what she paid for it) and be glad to get rid of the damned thing.

Okay, now that we know what we want to do, let's see how much "leveraging power" we can scrape up out of Betty's assets. The house has a value of $100,000—she owes $48,000, so that's $52,000 equity. The land's value is $125,000, with $28,000 owed; that's another $97,000. We said we would sell the land partnership for $50,000 cash (no profit), so all in all we've amassed $199,000. Let's take $1,000 out of her bank account and make it an even $200,000. We can leverage this into at least an $800,000 deal. That's a whole bunch of apartments, and Betty never dreamed she would be in control of that much money! To get a better picture, see what this looks like on paper in Example B.

Betty moves into an apartment in her complex, just right for her. She now has enough depreciation to more than offset income from her business, and now she can expand into yet another location like she wanted to. Where does the money come from? She borrows against her business, which is zero-leveraged.

COMING UP WITH EQUITY

As our last example, we have Tom and Edna, that delightfully young and carefree couple down the block. He's an engineer and she is a supervisor with the telephone company—both excellent jobs, producing a combined gross income of over $39,000 a year. Although there is a more than $3,200

Example A. Stanley White's Net Worth Statement

	Before	After
Assets		
Real estate	$60,000	$320,000
Savings	14,000	3,000
Stocks	8,000	8,000
Life insurance (cash value)	6,000	-0-
Auto	5,000	5,000
Pension fund	1,000	1,000
Total	$94,000	$337,000
Liabilities		
Loan (home)	-0-	$ 48,000
Loan (business property)	-0-	195,000
Total	-0-	$243,000
Net worth	$94,000	$ 94,000
Leverage	-0-	72%

cash flow passing through their fingers each month, they don't seem to be putting any of it aside. Tom and Edna live high and fast, and other than about $2,000 in the bank and $12,000 worth of sports cars, they're broke! "After six years of marriage, we don't have a damned thing to show for it. What we don't blow, we pay out in income taxes."

They seek expert advice, and it's pointed out that one step in the right direction would be to at least acquire a house for investment appreciation but, more than that, for interest and property tax write-offs. Where are they going to get the money for the down payment? Since they have every credit card imaginable, between personal loans there and perhaps against the cars, this poses no problem. They certainly can make any kind of payments with all their cash flow—kind of like a forced savings they both agree they need.

Tom, however, has a much better idea. Money is very tight right now, 18 percent and up when you can get it. Maybe the best move is to approach a seller directly on a contract or installment sale. By offering a little more than the seller hoped to get for the property, they may arrange 10 percent down instead of 20. It's a good deal for Tom and Edna as well as a good move for the seller when it comes to capital gains taxes. They decide to chattel mortgage the cars for the small amount of cash they'll need. (See Example C.)

Tom and Edna now have payment obligations (mortgage plus car loan) exceeding their previous rent. And since you can't depreciate a home like you can business property, they won't have that tax advantage. But their partner, the IRS, will still be helping them out; Tom and Edna can deduct interest payments on both the mortgage and the car loan, reducing their federal and state taxes by more than enough to offset the increased cash outlay. Could they have swung a duplex and come out even better? Probably so.

Example B. Elizabeth Bentley's Net Worth Statement

	Before	After
Assets		
Real estate	$100,000	$800,000
Land	125,000	-0-
Land partnership (liquid value)	50,000	-0-
Keough (self-employed retirement)	18,000	18,000
Auto	6,000	6,000
Savings	3,000	2,000
Business (incl. inventory)	85,000	85,000
Total	$387,000	$911,000
Liabilities		
Loan (house)	$ 48,000	-0-
Loan (land)	28,000	-0-
Loan (apartment complex)	-0-	$600,000
Total	$ 76,000	$600,000
Net worth	$311,000	$311,000
Leverage	19.6%	65.9%

Example C. Tom and Edna's Net Worth Statement

	Before	After
Assets		
Real estate	-0-	$85,000
Savings	$ 2,000	500
Autos	12,000	12,000
Total	$14,000	$97,500
Liabilities		
Loan (home)	-0-	$76,500
Loan (cars, chattel mortgage)	-0-	7,000
Total	-0-	$83,500
Net worth	$14,000	$14,000
Leverage	-0-	85.6%

GET MONEY TO MAKE MONEY

Our lessons learned are these: it takes money to make money; if you don't use it, you'll lose it; it's not how much you make, but what you get to *keep* that counts. Old adages? To be sure, but all with a grain of truth.

The middle- and lower-income people in this country do carry the major burden of the tax load. They never seem to be able to acquire the necessary *leverage* of equity to avoid taxes or are psychologically stunted in their financial thinking, causing frugal plodding-along reactions and losing ground every step of the way. Not to borrow money is *not* a thing to admire! The way you make money is to use someone else's. This is common business practice; all businesses (worth their salt) have borrowed since the dawn of time. To wait to save it is a nonsensical waste of both time and opportunity. Leverage and more leverage is the secret of success.

You don't have to leverage into real estate as our examples have illustrated. You can opt to be "born again free" and use the money for that business of your very own that you've always wanted, to seek and gain direct rewards from the benefit of your capabilities, rather than continue to be a pawn in the system that sometimes reeks of unfairness. Businesses enjoy all the write-off advantages of real estate and quite a few more. Then too, they have a greater span of accelerated profit potential—that is, you don't have to sit and wait for appreciation in value through inflation; you can get out and do something about the situation yourself. The same would be true of static versus dynamic income possibilities.

Whether you're a Stanley White, a Betty Bentley, or a Tom and Edna—or whether you don't fit one of those prototypes—the important thing to remember is that there exists for you an opportunity to take money you already have or will have. That money is slated now for income tax payments, but you can turn around, and with the IRS as your partner, invest in your future. ◻

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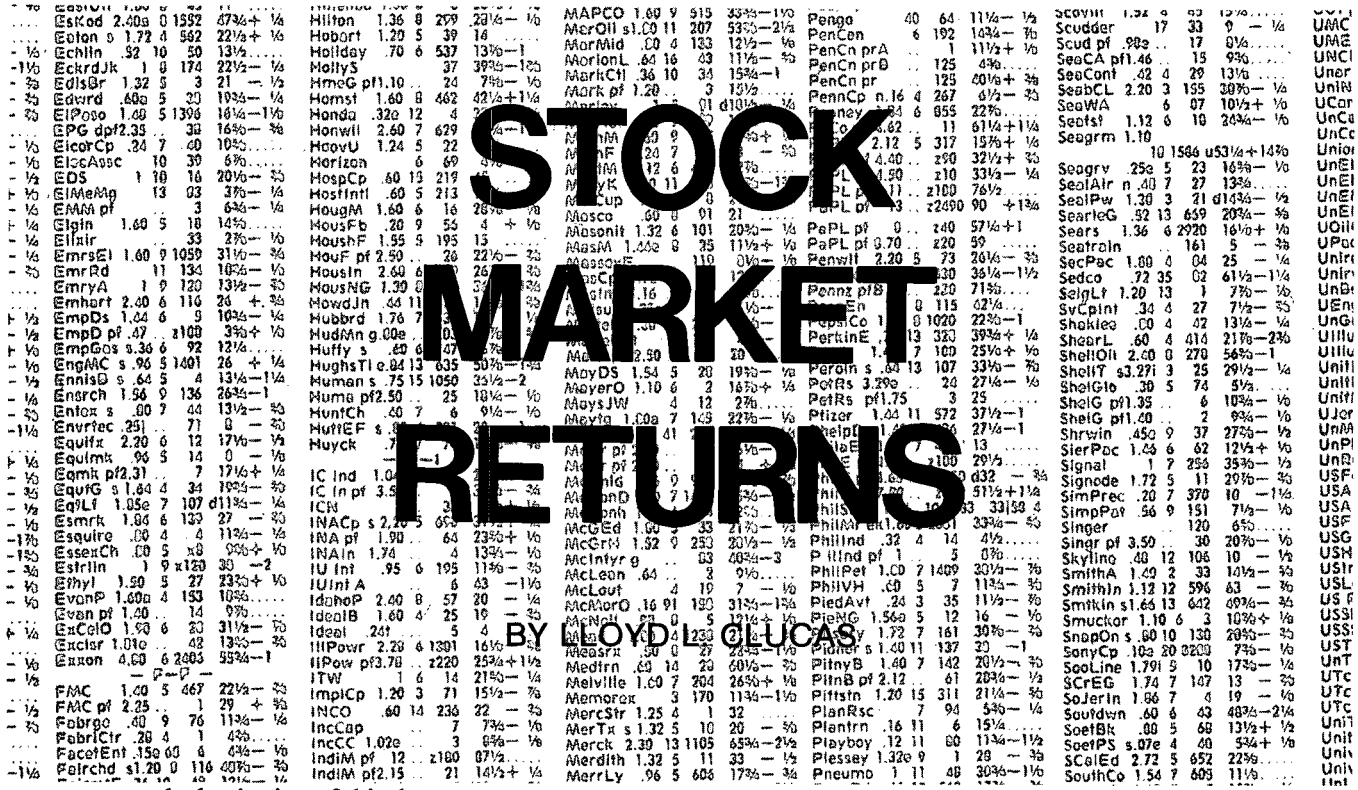

STOCK MARKET RETURNS

BY LOYD L. LUCAS

"The beginning of this decade certainly does not look auspicious. The omens are just about as bad as they were at the end of 1969, if not worse. This is no longer the season to be jolly. It is damn serious and we better have no illusions about it." So columnist Heinz H. Biel lectured readers in *Forbes's* first issue of the new year. Even though Mr. Biel is right, there's reason to be jolly—since 1969, a lot of folks have come to the same conclusion he has, and they've been taking adaptive action. The marketplace may not be efficient every day, but it certainly is by the decade.

Common stocks represent real assets as much as do oil, metals, and real estate — and the data suggest they're a good buy today.

The doomsday scenario is well known. Contrary-opinion practitioners should be looking at the stock market. Today the debates center on inflation accounting, investment incentive, getting corporate returns on equity up, cutting taxes, raising savings rates, adjusting taxes for inflation, and deregulating business. There is now hope and *some action.* There was neither in 1969. The 1980s look better for stocks than the decade just past.

I am here to follow up on my piece that appeared in REASON's June 1978 financial issue. In that article, I pointed out the good relative value showing up in the stock market and painted a bullish scenario into the mid-'80s. Rising intrinsic and relative values in stocks, positive changes in public attitudes, a favorable stock market cyclical environment, rising institutional and foreign buying power, and the general disillusionment with stocks formed the foundation for optimism. The article concluded on this note:

> *But while the millenium probably has* not *arrived, there nevertheless appears to be an excellent opportunity brewing right now in US equity markets. No other major country's economy or market looks as promising. When the time comes for holding shares of industrial enterprises, it would be a sorry commentary . . . if free-market believers were still off in the woods gathering nuts and berries.*

That was heresy at the time it was written (early 1978). Today this thesis has become the center of serious debate in the investment community, with vigorous advocates on both sides. So let's review the case for stocks in today's environment.

Contrary to general expectations, there was no recession in 1978 nor in 1979. Real growth continued to be generated, although at steadily diminishing rates of increase. The deterioration process for the economy has been slow. The incredibly bad behavior of the Federal Reserve Board during 1978 and 1979 accounts for the new high inflation and interest rates achieved in 1979. Consumer confidence levels deteriorated in 1978 and *collapsed* in 1979. Inflation-adjusted corporate earnings probably rose in 1978 and probably fell in 1979—inflation adjustment is imprecise. Corporate dividend growth outpaced inflation in both 1978 and 1979.

Against that background, how did stock prices do? Remarkably well—especially if the recession many expect is right around the corner. Table 1 shows the results for several stock price indices. While risks have risen with stock prices since early 1978 and inversely with the decline in the economy's vigor, a strong case for common stock investing can still be made.

WHERE STOCKS ARE HEADED

The doomsday litany is well-known. Earnings and profits are up sharply for the prophets of gloom and doom. Scary seminars are a booming business. The evening news carries the price of gold. The public's confidence has *already* fallen sharply. This isn't to say that attitudes can't get worse; they

can. It merely means that the marketplace is not dominated by starry-eyed dreamers unaware of the very real political and economic problems the market faces.

Stock prices still look reasonable compared to earnings. Table 2 plots the ratio of Standard & Poor's 500 stock price index over the Commerce Department's computation of constant-dollar earnings for US nonfinancial corporations. They are not fully comparable. They are, however, as good an approximation as we're likely to get until the constant-dollar earnings numbers that will be coming out soon for many large companies can be put together for some major market average. The earnings numbers are approximations only. They are a crude form of inflation adjustment.

Table 3 makes the same sort of comparison, using the Indicator Digest Average (all NYSE, geometric average, unweighted) instead of the S&P 500. In both cases, at the end of 1978 stock prices do not appear high compared to purchasing-power-adjusted earnings. Stock prices, however, were up and constant-dollar earnings probably down some in 1979. Therefore, whatever "undervaluation" may have existed at the beginning of 1979 surely diminished somewhat by the end of the year.

Central value computations suggest that stocks in general are reasonably priced. Using (*a*) book values, (*b*) normalized earnings, (*c*) implied growth rates, (*d*) dividend yields, (*e*) trend inflation rates and bond yields, (*f*) historical price-times-earnings (P/E) ratios adjusted for inflation, and (*g*) regression formulae utilizing historical relationships and estimates for next year's results, stocks in general seem priced at or somewhat below "central value." Expected growth for the Dow Jones Industrials is subnormal and has been for some time. They have been (and are) especially vulnerable to a hostile political environment. They are cyclical and highly visible. Many of their markets are in slow-growth areas. Nevertheless, our estimates of central value for the DJIA in 1980 fall in the 865-885 range, right about where they are at this writing.

Less-mature large companies are estimated to have central value levels 15 percent above the DJIA's P/E ratio. For the sort of growth most investors should be looking for today, at least a 28 percent premium over the DJIA may be expected at central value levels. In general the DJIA looks centrally valued, the typical large company slightly undervalued, the good smaller growth companies somewhat undervalued, and small high-technology companies clearly overvalued. On balance, the values for the next several years look quite reasonable—not cheap, but reasonable.

A sharp market decline would be required to produce many truly undervalued situations. Such a decline would also establish a bullish washed-out psychological condition that presently does not exist in the market with the DJIA in the mid-800s. The DJIA at 650-700 would probably accompany such a condition. A Federal Reserve-induced credit squeeze would be the likely prime mover for such a market break.

BUSINESS HELP

Corporations are adjusting to inflation. Freer interest rates have combined with financing ingenuity to permit more facile management of corporate financial needs. Items such as overnight repurchase agreements have become widely used. More-flexible money markets have permitted corporations to function with lower cash balances.

Inventory management has improved. More and cheaper computer power has been the key here. Companies can function with less capital tied up in inventory. A feature of the 1975-to-date economic expansion has been tighter inventory control.

Escalator clauses are getting into all kinds of contracts. Fewer companies are getting boxed into fixed-price contracts where inflation may eat them alive. Pricing policies are getting better. Once again, computers are helping management respond faster to the need to raise prices to offset cost increases. Companies are coming to realize that cost increases can be large and permanent.

Accounting practices are more and more seeking to show inflation's effect. The outcome here may be less taxes paid (as in shifts to LIFO inventory accounting), more realistic earnings reports, heightened corporate realization of inflation's effects, and increased political pressure for lower taxes. Efforts at inflation accounting are also showing that manageable debt is a good thing to add to the balance sheet when inflation is expected to persist.

Return on equity is becoming the major focal point in corporate planning. Maintaining it is the basis for sustainable corporate growth. It is a tough job when inflation is accelerating. A company's capacity to raise prices without getting attacked by the government, beaten by the competition, or having its market shift to a substitute product is essential. Having a separate market niche and being the low-cost producer of a product are often crucial. More and more companies are emphasizing return on equity and doing a better job with it

Table 1. Stock Price Index Changes (Approx.)

	1978	1979
IDA (unweighted; all NYSE)	+1.3%	+19.7%
Wilshire 5,000 (weighted by capitalization)	+5.6%	+19.3%
Value Line 900 Industrial Composite (weighted by capitalization)	+9.1%	+18.3%
S&P 500 (weighted by capitalization)	+0.8%	+12.3%
DJIA (weighted by price)	-3.3%	+ 4.2%

Table 2. Ratio of S&P 500 Stock Index to Constant Dollar US Nonfinancial Corporate Earnings (USDC)

(Dec.) 1965	1.00
1968	1.28
1974	.89
1977	.88
1978	.75
1979	(est.) > .90

Table 3. Ratio of Indicator Digest Average* to USDC

(Dec.) 1965	1.00
1968	1.53
1974	.44
1977	.56
1978	.50
1979	(est.) > .65

* NYSE common stocks, geometric average.

than they did 5 or 10 years ago. Table 4 shows the return on equity for the Value Line 900 Industrials, dominated by large corporations. And for all corporations, return on equity rose from 12.4 percent in the first quarter of 1978 to 18 percent in the second quarter of 1979. Net margins on sales rose steadily to a 6.1 percent rate in mid-1979. These are both above the averages for the past decade.

Corporate stock prices, earnings, and dividends have a good record against inflation. Prior to 1968 it is clear that stocks delivered a sizable advantage over bonds, other fixed-income media, and the inflation rate. From the end of 1968 through the end of 1978, stock prices did rather poorly on all counts. Stocks were clearly overvalued in 1968. Rising inflation demands a higher discount rate and hence a lower general market P/E ratio. That pushed total stock market returns down sharply.

Nominal earnings and dividends held their own, however. Using the Value Line 900 Industrial Composite statistics, nominal earnings, deflated by the Consumer Price Index (CPI), scored a 29 percent gain for the 10-year period. Dividends, deflated by the CPI, increased 4 percent—nothing to brag about, but better than some people realize. It is true, of course, that inflation does cast some serious doubt on the reality of the earnings numbers themselves. Simple deflation by the CPI is not a complete or adequate adjustment for inflation's effects on profits.

Table 4. Value Line 900 Industrial Composite Return on Equity

1979:	(est.) >14.5%
1978:	14.6
1977:	13.4
1976:	13.3
1975:	11.4
1974:	13.8
1973:	13.5
1972:	11.4
1971:	10.5
1970:	9.8
1969:	11.7
1968:	12.1

Between 1968 and 1974, the market really *discovered* inflation. That was the shock period. We now seem to be in the period when P/E ratios are stabilizing somewhat in reasonable areas. Earnings and dividends should play a somewhat larger role in equity returns from here forward (barring a hyperinflation), and that would be good news.

THE STOCK OPTION

The flight from paper currencies continues. In fact, it is accelerating. A good deal of the present mania is a product of foreigners' political fears, as in the Mid-East. Nevertheless, more and more people are discovering inflation and its effects. A dollar one year hence is no longer a dollar. It no longer serves as a storehouse of value. A half-century of thrifty tradition is going down the tubes. Consumer credit is rising relative to incomes. Personal saving fell below 5 percent in 1979. In only four years since 1946 has it been as low. Unlike pre-1976, the consumer is now betting on the continuation of inflation. Defenses are houses, gold, buying now, borrowing, and money market funds.

The avalanche of money that has moved by the billions into money market mutual funds is testimony to the awakening among investors. Soon they will realize that that money isn't going to keep up with inflation on an after-tax basis there, either. These investors will eventually be drawn to equity ownership of profit-earning assets. Lending is a loser's game for taxpayers in an inflationary environment. Too many competitors are tax-free institutions that can offer better terms, in larger volume, than can the individua taxpayer.

Inflationary momentum is great. It is likely to persist at high rates, though it may stabilize somewhat this year. In a presidential election year it is questionable whether the Fed will jam on the monetary brakes. If they do not, the flight from currencies will continue. Stocks will be a beneficiary. A recent *Wall Street Journal* article noted that "frantic precious-metals buying overseas has ignited an equities-buying spree on the Tokyo Stock Exchange as Japanese investors try to hedge against inflation." That takes on added significance when we realize that P/E ratios in Tokyo are already over 20, versus around 8 in the United States.

Common stocks represent assets and real values as much as do oil, metals, and real estate. Reading many discussions of inflation hedges would leave you with the idea that common stock certificates were little more than personal IOUs from the Flim Flam Man. Some are; most are not. Some coins are counterfeit, too. The assets and earning power behind a stock certificate are quite real. No matter the real asset you want, there are usually available plenty of stocks backed up by that particular item as an *earning asset,* not just a "rustable." In early 1980 metals and oil are the big deal; later in the year it may be something else. And not all worthwhile assets have to be things you dig out of the ground. A fine marketing organization is worth plenty any time. Of course, if the monetary brakes are applied, the most popular inflation-hedge assets will likely fall in price.

Discussions of inflation hedges leave you with the idea that stock certificates are little more than IOUs from the Flim Flam Man.

Corporations engage in a value-adding process as they manage assets. Good management is what gives the stock owner the chance for returns above the rate of inflation. You don't get that with ownership of only the tangible asset itself. There is no going-concern value in an ingot of silver. It takes fear and panic or just plain tomfoolery to obtain a longer-term rate of return above inflation by putting a tangible asset (comic books?) in your attic.

Common stocks are more convenient, have lower transaction costs, and are less risky for most individuals than are most other investment vehicles. Bid-asked spreads are narrow. Liquidity is good. Diversification is easier, since ownership interests are divisible. There is considerable information available about the businesses the stocks represent. Commissions are low. Fraud risks are low. At least all this is true compared to most direct-ownership or other esoteric inflation hedges.

STOCKS: GET IN LINE

Massive buying power has accumulated on the sidelines. Through 1977 and 1978 institutions ran up large cash balances. Common stock mutual funds were running over 10 percent of assets in cash. Merrill Lynch surveys

showed 14-16 percent cash positions for institutional investors. For 1978, it is estimated that only 17 percent of all new money coming into private pension funds was invested in common stocks. That was down from 50 percent in the early 1960s and over 100 percent in 1971-72. The flight from equities has been sizable. Stocks are now estimated to be only 55 percent of pension fund assets. Bonds make up most of the rest.

That is already changing. In 1979 new pension money went into stocks at around a 50 percent rate. The Merrill Lynch survey for the fourth quarter of 1979 shows about an 11 percent cash position for institutions. That is still historically high but down from last year.

And now GM, in what augurs to be an important move, instructed its pension managers in late 1979 to shift their pension investing from 50 percent stock and 50 percent bonds to 70-30 in favor of stocks. And it's about time. Fixed-income securities during inflation could not help GM reduce its contributions to its pension funds. Common stocks may.

Institutional managers have been hiding in stock index funds, bonds, option writing, or anything else that would let them recover from the 1973-74 slaughter they endured in stocks while inflation was being discovered. Now they are coming out of their bomb shelters to fight back. As the GM decision highlights, the clients are goosing their managers along. So now the hard evidence is beginning to appear in support of our early 1978 thesis. A revolt among the beneficiaries of "fixed income" contracts such as some pensions, and most life insurance, may hasten the move from bonds to stocks.

The rationale isn't difficult to follow. Earnings and dividends grow. Bonds move in the opposite direction from inflation. Their interest payments do not grow. Inflation grows.

This outlook is *nowhere near* a universal one on Wall Street. Many institutions are still busy trying to time their purchases in the bond market. That's like chasing the greased pigs at the county fair—it may be fun, but it is messy and not very productive.

Those pension fund bonds just sit out there doing nothing for the corporate pension fund sponsor. In fact, they may offset some of any inflation advantage the company may have otherwise gained from being a net monetary debtor.

The huge increase in money market funds is clearly, in part, a build-up of individuals' buying power. Eventually, much of it is likely to be tempted into equity ownership as inflation grinds away on the taxable individual.

Finally, there are the foreign investors. As the electronic age arrives, all major investment markets are becoming international. Prices are not only being set "at the margin," but increasingly that margin is controlled by flows of foreign investment funds. The Securities Industry Association reports that over the past five years foreign buying has accounted for 20-25 percent of net purchases of US stocks. Such buying activity tends to parallel the performance of the US dollar against other major currencies. The dollar made a low in October 1978 that has not been breached to date on a trade-weighted basis. And as international political turmoil increases, the relatively safe and relatively self-contained US markets are likely to become more attractive to foreign money.

COMPARATIVE ADVANTAGES

The value of common stocks relative to other investment vehicles is rising. Many "inflation hedges" have done admirably over the past five years. Insofar as they have advanced well in excess of price inflation, most of them are likely priced over their "intrinsic value." Take gold and single-family houses as examples.

Is an ounce of gold really worth 150 bushels of wheat? Perhaps. Or maybe wheat is underpriced. But at current levels, gold clearly has turned into political turmoil insurance more than the sensible inflation hedge it used to be. As Milton Friedman assessed it recently, if gold were priced solely on the basis of US monetary mismanagement, it could be in the $200-$225 range, and not at the $700+ level. That seems reasonable.

The single-family house has been a great inflation defense, but it has been rising in excess of the inflation rate for quite a long time now. That cannot be justified on any intrinsic value basis. Relative to stock prices, there have only been three other times in the past 100 years that stocks looked so good relative to houses: 1894, 1921, and 1949. Nor is real estate a one-way street. Consider LaSalle Street in Chicago's financial district: 1919: $100/sq. ft., 1967: $69, 1977: $138. Or take Chicago's State Street (that "great" street) in the downtown area...please! 1929: $170/sq. ft., 1967: $145, 1977: $122.

Value-oriented investing is returning to favor. The beating taken by investors in the early 1970s has prompted a relative return to more fundamental investment valuation techniques. There is still a lot of herd-following going on, but the resurgence of value investing, while it lasts, works toward more rational pricing in the stock market, and that's bullish for longer-term, value-oriented investors.

Corporations continue to show the way with their acquisitions of other companies. While other reasons intrude on the decision to acquire, the corporate takeover spree is undoubtedly prompted in large part by the belief that the earning power of many publicly traded companies far exceeds the prices their stocks command in today's market. These decisions are being made by the same managers who are still letting their investment advisors put bonds in the company pension fund. Many of them are likely to follow GM's lead toward more stock and less bonds.

THE BASIC TOOLS

Accelerating inflation:	gold/realty
Decelerating inflation:	common stocks
Stability:	common stocks
Decelerating deflation:	common stocks
Accelerating deflation:	cash/safe fixed income

High expectations are drawing plenty of stock buyers. Despite the gloom and doom and the sluggish DJIA, the market moves when expectations rise. The booms in high-technology issues and energy stocks have been notable. Many stocks here already appear overvalued. Fear rather than solely greed seems to be a prime mover in today's market. But a mover it is; witness the mining and defense stock gains during late 1979 and early 1980.

The point here is that, as an understanding of equity values reaches more investors and fear of inflation grows, fuel for the market will be forthcoming. The stock market is not dead. But neither is it particularly efficient in recognizing value beyond next month.

(*Continued on p. 59.*)

TRIMMING YOUR HEDGES

Why are so many people eager to swap their "valuable hard assets" for your "lousy paper money"?

BY ALAN REYNOLDS

IF I SAY THAT THE WORLD ECONOMY is going up in flames, people invariably want to know whether they should invest in matches. Many even buy books on How to Prosper During Rotten Times. Obviously, we can't all prosper in bad times, or they wouldn't be bad. All such advice is necessarily based on the unlovely idea of profiting at someone else's expense, which can't work when everybody's trying it. With all these bestsellers telling millions of people to buy something cheap and sell it to someone else at a higher price, you have to wonder who will pay that higher price and where he'll get the money.

Even the time-honored practice of buying one another's houses at progressively more absurd prices begins to look a bit shaky in my suburb. The next round of eager buyers has forgotten to show up.

Somebody advertises some dried figs that he says will become infinitely valuable in the next Stone Age, while your Federal Reserve notes, he advises, will be used to light the wood stove. The question is, why are these fellows so eager to swap valuable figs for your lousy money?

The key to understanding the current situation is that this is a fully anticipated inflation; there is no hint of "money illusion." Although inflation is never enjoyable for long, it is no fun at all when it is widely expected. An unanticipated inflation can sometimes stimulate business for a while, because prices rise faster than wages, and debts can be repaid in shrunken dollars. In the topsy-turvy world of anticipated inflation, however, orthodox fiscal and monetary measures to "stimulate" the economy just make people expect more inflation. The resulting rush to borrow drives interest rates up; wage rates and commodity prices soar; and the dollar sinks.

Inflation when it is fully anticipated has effects very different from when it is widely underestimated. In an unanticipated inflation, wealth is transferred from creditors to debtors or, more precisely, to those whose monetary liabilities (such as mortgage debt) exceed their monetary assets (such as bonds or money). Unanticipated inflation in effect taxes people in proportion to their claims on some fixed amount of money, with the gains going to those (including the government) whose debts constitute that money. If prices somehow doubled unexpectedly, for example, homeowners would experience a doubling in the value of their homes with no rise in mortgage liabilities, while mortgage lenders would find the real value of their corresponding monetary assets cut in half.

A fully anticipated inflation, however, creates eager borrowers and reluctant savers, driving interest rates up enough to roughly compensate for the expected inflation. Businesses and individuals attempt to evade inflation by taking on monetary liabilities (debt) and switching from monetary to real assets (such as houses, commodities, and durable goods).

Instead of responding to increased inflation by reducing debt and increasing savings, as was typical in the past, consumers have been trying to beat inflation by vigorously accumulating houses, consumer durables, and an endless variety of tangible objects that are expected to increase in value more rapidly than the average rate of inflation. The process has been fed by large doses of money and credit, enabling people to buy now against expected future gains in income and wealth—gains that may not materialize. The high ratio of debt to income leaves consumers quite vulnerable to any slowdown in income or to any softening in the value of homes and other assets.

Conventional data fail to capture the full scope of consumer inventory accumulation, because much of it occurred in casual markets for scarce goods produced in the distant past. The "antiques and art" section of the classified ads of any newspaper conveys some flavor of what is going on. The extraordinary price increases for many of these things are another indication of where the dollars are flowing. In the past decade, such things as coins, stamps, old masters, and Chinese ceramics have risen at two or three times the average inflation rate.

Spending incomes on ancient objects is of little help to producers or merchants of new consumer goods, nor does it add to the nation's capacity for future production. For every buyer of an Oriental vase or rug, there is, of course, a seller taking his money, and perhaps the seller then buys a car or a corporate bond rather than another vase or rug. But the apparent net diversion of demand into scarce objects, for both consumption and investment purposes, nonetheless involves a relative redistribution of purchasing power toward uses not commonly thought of as productive. The shift of investments from financial to real assets also increases measured inflation, because the prices of financial assets are not included in our price indexes. If the prices of bonds fall and the prices of houses rise, conventional statistics only notice the increase.

Like any excessive accumulation of inventories, the excessive accumulation of consumer inventories is inherently unsustainable. Buying now to avoid future price increases implies buying less in the future. Buying things to hedge against inflation can only continue as long as others are willing and able to continue to bid the affected price up (the notorious search for a "greater fool"). A significant reversal of consumer inventory accumu-

lation could come about because of financial constraints or disappointment regarding gains expected from the sale of houses, beer can collections, or whatever.

When people expect very high inflation, it requires interest rates well above the anticipated inflation rate to damp the demand for credit and slow the growth of money. The situation is compounded by the sharp erosion of liquidity in business and banking, which spurs the demand for lendable funds while limiting the supply.

With higher inflation, it takes larger increases of money and credit to finance the same amount of real activity. That is, inflation erodes the real purchasing power of people's money balances. Yet faster money growth would feed the spending that fuels more inflation, in a dangerous upward spiral. One conspicuous constraint on the process is the depreciation of the dollar in foreign exchange markets, which appears to inspire somewhat greater efforts toward monetary restraint than does the related shrinkage of the dollar in domestic markets. The Federal Reserve cannot continue to feed money to the inflation because foreign holders of dollars simply will not put up with it.

Whether instituted for domestic or international reasons, a sharp slowdown in the rate of growth of the money supply would soon produce a comparable slowdown in the growth of income and spending (nominal GNP). Because of long-term contracts and other rigidities, costs would continue to rise rapidly for a while, although softening markets would make it impossible to pass these costs along in higher prices. The resulting squeeze on profit margins would reverse the previously rapid growth of employment and labor income, thus undermining one source of the consumer boom.

All of the myriad threats of economic reversal are rooted in inflation and can scarcely be remedied by orthodox "stimulative" fiscal and monetary policies, which would simply aggravate inflationary expectations and the related excesses. Indeed, a credible, sustained shift toward fiscal and monetary restraint, although introducing temporary risks of its own, might well have some paradoxically beneficial effects through strengthening the dollar, bolstering stock prices and stockholder wealth, lowering inflation expectations and related costs (including long-term interest rates), and easing the financial strains of heavy Treasury borrowing.

There would, however, be some disappointed investors if we experienced a sharp slowdown in the growth of money and spending. Many homes and scarce objects have been purchased in the expectation of being eventually resold at a handsome profit. The expected increase in wealth had a powerful impact on consumption. People even borrowed against unrealized capital gains, taking second mortgages on the basis of paper gains in order to remodel houses or buy furniture. These wealth effects on consumption are strongly dependent on continued high inflation. A slowdown in total spending and reduction of inflationary pressures could be expected to unravel the whole process of consumer hedging and speculating. People would then become less willing or able to take on sufficient debt to support continued price increases, because their expected gains in family income and employment look less promising. That price resistance, in turn, would make existing owners of homes and other supposed hedges feel less wealthy, thus fostering further consumer retrenchment and rebuilding of liquidity.

It must be remembered that most hedges against inflation share the cyclical volatility of commodity prices in general, with prices falling sharply in recessions. And nothing will serve as a superior hedge against inflation if the present price currently discounts that prospect.

The housing market has already discounted an enormous amount of future inflation and incorporated that expectation into present prices (and interest rates). People have bid housing prices up by borrowing against expected future inflation of their nominal incomes, thus translating considerable future inflation into present housing prices. If some housing prices reflect more inflation and earnings growth than will actually occur (as is likely for at least the cyclical downturns), then the disappointment regarding expected wealth would tend to provoke consumer cutbacks. Housing prices did not keep up with general inflation in 1970 and 1974; that is, the real value of the housing stock fell. Gold prices in the last disinflation were cut in half.

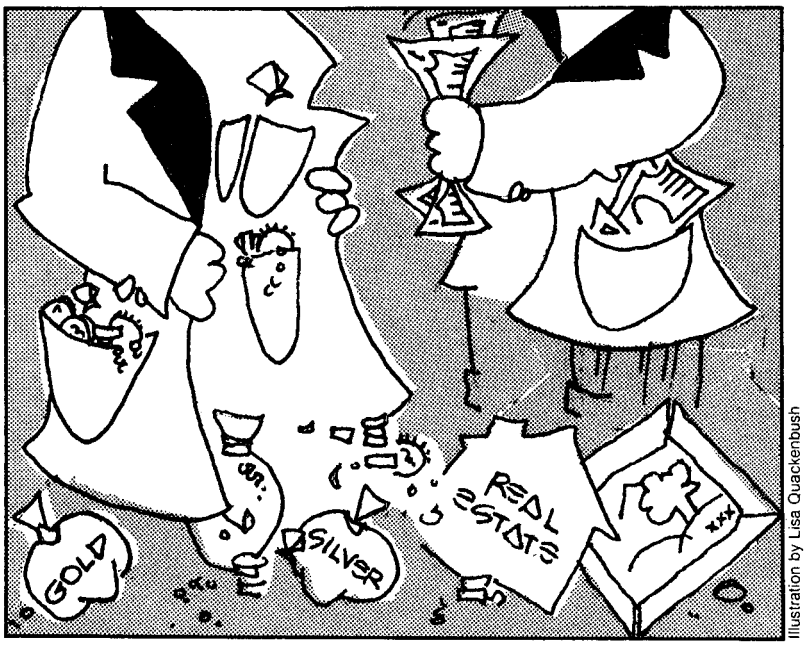

Illustration by Lisa Quackenbush

It is generally understood that financial markets are efficient, in the sense that prices of financial assets at any moment accurately reflect the best available information about their future value. Unfortunately, the lesson is not often applied to markets for real assets, where many people are easily persuaded that current prices can remain perpetually too low (to reflect the asset's value as a hedge against inflation). But the demand for tangible assets has been strong for some time, so current prices of such assets already incorporate a lot of expected future inflation.

In a world of perfectly anticipated inflation, there could be no sure hedges against inflation, because current prices would already discount that prospect. Expected inflation increases the demand for "hedges" and drives up their price. The switch from

financial to real assets weakens prices of the former and bids up prices of the latter. At some point in this process, financial assets have to become at least relatively more attractive than real assets, even as hedges against inflation. Real assets can't always be the better bargain, regardless of price. Speculation on continued rapid price increases has to get more risky the more the price has already risen (unless expected inflation goes higher and higher).

At the very moment you read this, the price of, say, gold and silver is neither too high nor too low. In the absence of shocks or surprises (and aside from some important complications concerning taxes), the prices of both real and financial assets should tend to rise at about the prevailing rate of interest. If expected future inflation goes up, there will be another upward revaluation of real assets and a downward price adjustment for stocks and bonds. If expected inflation goes down—just to a lower rate of increase—financial assets are apt to gain at the expense of tangible "hedges."

Skepticism about inflation may well be warranted, and that attitude has certainly paid off during most of the past decade. But periodic gestures toward slowing inflation do occur and can make long-term hedges a poor short-term investment. It is not enough to argue, while the hedge asset's price is falling, that the price is sure to go back up over a period of years. If the price (less dealer fees) does not rise as fast as the rate of interest, there is an opportunity cost involved in not selling the asset and investing in something else.

There is a time and place for everything, and this may not be the best time to be getting into hedges, regardless of past success. ◻

Alan Reynolds is vice-president for economic research at a major US bank. His Viewpoint column appears in REASON every third month, and he frequently graces our pages with articles and book reviews.

Pastor

(Continued from p. 39.)

your entire investment. A pure developmental drilling program, on the other hand, is a relatively low-risk venture with a very high probability of realizing a good return on your investment. But then, the profit margin will be relatively low, too. The reason for this stems from the greater costs involved. As a result, few public drilling programs are purely exploratory or purely developmental.

DIVERSIFYING RISK

The balanced drilling programs are either designed to provide a 50-50 split between exploratory and developmental drilling or tend to be biased 65-35 toward either exploration or development. The intent of the balanced program is to maximize the tax write-offs and give the investor an opportunity to participate in a new discovery and, at the same time, protect the investor's capital through developmental drilling activities. The expectation is that, even if the program completely strikes out in its exploratory activities, the developmental wells will generate enough to recoup one's investment. Major brokerage firms select a few public drilling programs each year from among the 60 companies that raise money publicly. As a rule, if a drilling program is offered through a major brokerage company, it has been pretty thoroughly checked out.

When selecting a public drilling company, it is advisable to choose one that is large, consistent, and preferably a major factor in the industry. It is also a good idea to invest in one that drills *only* for the partnerships it manages. This will avoid conflicts of interest. You would also be better off avoiding companies that charge back acreage costs to the limited partners if the acreage proves to be worthless; it is wiser to choose a company that treats the acreage as part of its capital contribution to the program.

As a rule of thumb, the rate of return on an oil drilling program investment can be considered a success if you receive back your original investment in three to five years and a steady tax-favored cash flow thereafter. Your odds of being successful will be improved by sticking with seasoned public drilling companies that have demonstrated the capacity to successfully manage a number of drilling programs for five years or more.

To minimize the risks of these investments, it is advisable to participate in each program over a three- to five-year period. There are several advantages to doing this. First of all, you have a far greater opportunity of participating in an exceptionally successful program. Some of the programs will be mediocre, some of them will be good; but all you need is one spectacularly successful one during those three to five years to make the entire endeavor well worthwhile. Second, by participating in a series of programs, the cumulative tax advantages accrue to your advantage. Let's assume that each program will enjoy a 100 percent write-off. As an example, if you have a first-year deduction of 75 percent on your investment and a 25 percent residual write-off the second year, that 25 percent carryover will dovetail with your next year's 75 percent write-off from the second program for a total 100 percent deduction. Third, you have greater diversification of risk by participating in a series of programs over several years, eliminating the one-shot nature of an investment in a single drilling program.

A public drilling program may be suitable for you in terms of your investment objectives and financial qualifications. You must, however, consider whether you are prepared to assume the risks, the illiquidity, and the long-term commitment required for such an investment. Perhaps the oil income program would be better for you given its lower risk, greater certainty of current income, and liquidity. Then again, you may wish to simply buy stock in oil-rich corporations. Whichever way is appropriate for you is, of course, the way to go. If you can diversify your capital into all three areas, you are only expanding your opportunities to participate in the potential rewards of investing in undervalued oil reserves. You too may become convinced that black gold glitters brighter than the precious yellow. ◻

Ray Pastor works for a securities firm in Hallandale, Florida, where he specializes in financial planning and tax-advantaged investments. He is currently working on his first book, on profiting from inflation.

Clucas

(Continued from p. 55.)

Random-walk/efficient-market proponents to the contrary, such values exist.

UPSIDE FACTORS

Cyclical market trends are positive. Five out of seven selected identifiable stock market cycles of four years' duration or more appear to be headed up at present. These cycle calculations are crude and imprecise. Their causation is unexplained. But with the recent popularity of the 50-year Kondratieff Wave, which is said to be pointed down, it seems appropriate to point out that the cyclical picture for 1980 and 1981 looks rather good.

Social and political attitudes in the United States are continuing to change positively for investors. This is a long-term element. The momentum still remains with those who favor more government rather than less, but they have lost the initiative in the marketplace of ideas.

Deregulation as an issue is still alive. It is a focal point of debate. A strong congressional vote in the face of a threatened Carter veto moves forward the FTC containment bill that may finally put a few checks on the wholly irresponsible Federal Trade Commission. Pass the sugar-frosted flakes! The trucking industry is also likely to get a bit more deregulation than it wants. Executive cries to the contrary, deregulation is good news for the kind of companies you should own.

State and local government spending recently fell as a percentage of GNP for the first time in 30 years. Progrowth forces are even making progress in Massachusetts.

The tax revolt also survives. The capital gain rate was cut in 1978; so was the corporate income tax rate. Some good tax-reduction bills are in the congressional hopper right now. Proposition 13 action in the states is still alive.

Of course, all is not well in any nation where the evening TV news on the economy always features an interview with a politician and/or an anti-big-business piece. It's like going to the zoo solely to look at the rats and hyenas—every time. And the citizenry is tuning out.

Recent public opinion polls are confirming my 1978 thesis. They indicate that the key thing desired today is stability. People feel out of step with the political system. The populace is sobering up. That's bullish for business. Contrary to my expectations, Carter did not bridge the gap. He made it worse. It was Congress that showed more responsiveness to the public mood, not Carter.

Even just from late 1978 to late 1979 big opinion shifts showed up. Concern about caribou is fading as the desire for energy takes precedence. Since 1976 there has been a trend in opinion toward more military spending.

Rising stock market values are creating a very positive technical potential for the market. The following is not a forecast. It is merely an outline of a plausible series of events and conditions that could help push stock prices to higher levels.

Executive cries to the contrary, deregulation is good news for the kind of companies you should own.

- General speculative excesses are squeezed out of the market (1968-74) but not out of the economy.
- Major stocks essentially move sideways for 15 years (1964-79); earnings and dividends rise.
- Companies discover, then learn to cope with, inflation.
- Eventually, rising values push stock prices up out of their long "consolidation" phase (where value was catching up to price).
- Suddenly, virtually everyone holding stock has at least a nominal profit, not a loss.
- Attitudes about stocks change from negative to positive.
- Stock prices soar.
- One possible prime mover: the assumed soaring value of the assets a company has in place; the imprecision in ascertaining that value aids hype-jobs by brokers.
- Soaring stock prices give the economy a lift; everybody feels like a winner.
- A speculative binge (in "asset plays"?) brings the entire market to a very vulnerable overvalued level from which a whiff of deflation could precipitate a crash. About this time in the cycle you would hear trademarks being discussed as "asset plays." And statements such as: "*People* are our most important asset. How can you even put a price on them?"

My response would be something incisive like, "Well, uh, exactly!" while on my way to call my broker. The selling season would be upon us. ◻

Lloyd Clucas is a lawyer who regularly writes on the US and Japanese economic situations. His investment experience dates from 1963; his investment advisory work, from 1974.

Coming Next Month:

- **Robert Ringer Interview:** Bestselling author of *Restoring the American Dream* talks about his book, his politics, influences on his thinking . . .
- **Transit Troubles:** Every city seems to have them, and traditional "solutions" have made things worse. Now, free-market alternatives are showing the way out of the mess.
- **Build a Better Bus:** Uncle Sam thought he could do it—but no one's beating a path to his door for it.
- **Unthinkable boycott?** People have stayed away from the Olympics before, and they ought to do so again, says a dissident Soviet writer.

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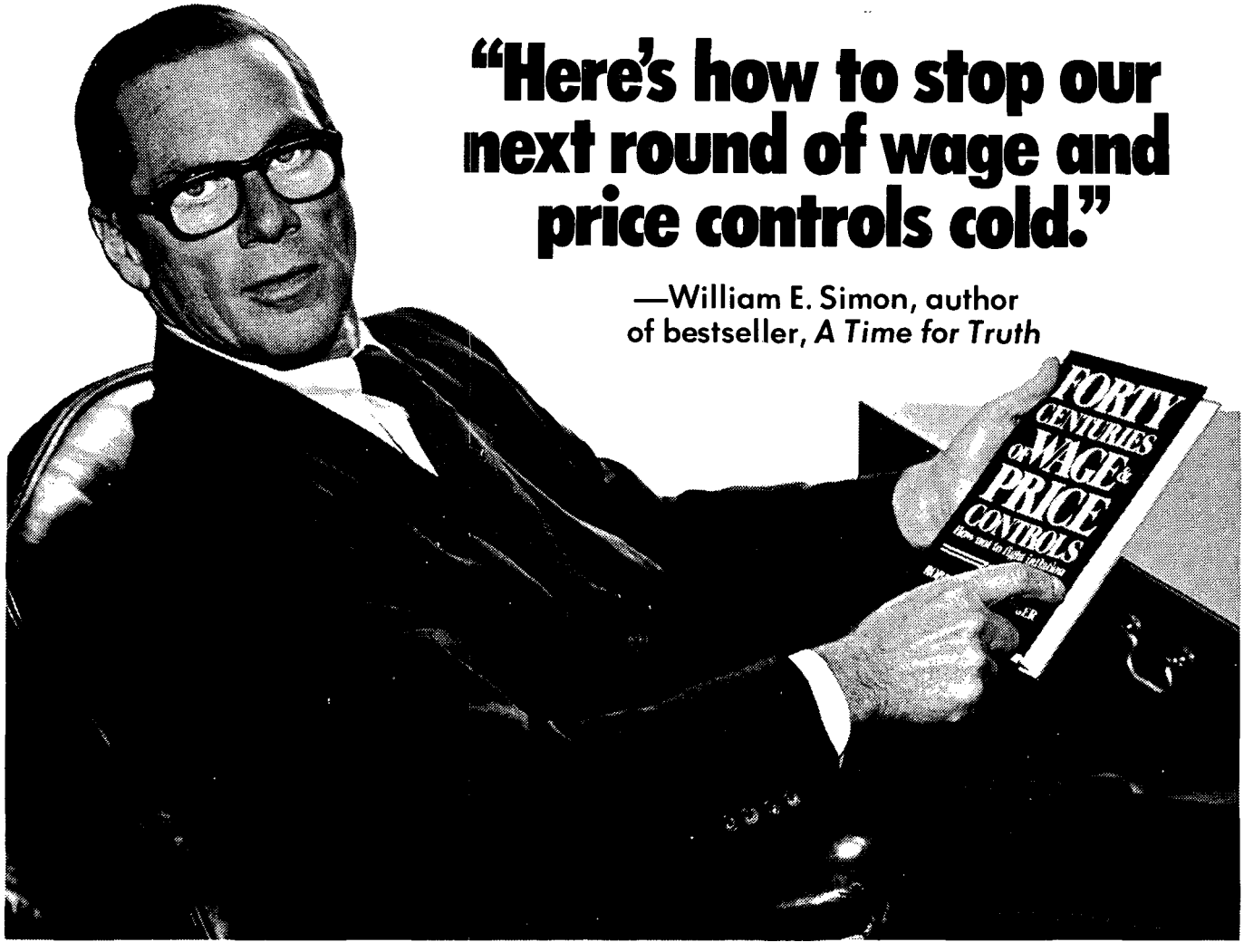

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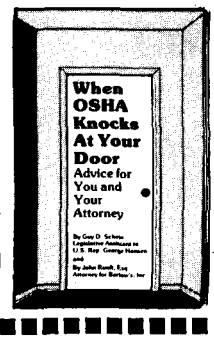


Carter, Pain, and Inflation

viewpoint

Murray N. Rothbard

Pain—*our* pain, of course—has been a constant theme of Jimmy Carter's since he burst on the national scene. During the 1976 campaign Carter assured us that "Ah feel yo' pain," and such is his enthusiasm for this empathy that he has gone out of his way to inflict pain ever since. After he went to the mountaintop last summer to receive his revelation on energy, he proceeded to remind us of his "pain" motif and then to scourge us for the mortal sin of wishing to buy foreign oil. His fellow born-again Christian, John Anderson, has been earning plaudits from the pain brigade for his high courage of wishing to inflict a 50-cent-a-gallon gasoline tax.

Now the old maestro of pain is back again, with his "comprehensive anti-inflation package" of March 14. Inflation, continuing for over two decades, has accelerated dramatically under Jimmy's ministrations and is now approaching the banana republic mark of 20 percent per annum. So Jimmy has decided to take off the gloves. It's "no more Mr. Nice Guy"; the time has come for stern measures, for "discipline" and especially—you guessed it—"pain."

The theory of the Carter administration, like all other administrations before it, is that inflation is some form of mysterious social disease, an epidemic among the American people. The job of the government is, like a white knight on a fiery charger, to go out and do combat with this dragon, to fight the disease. The theory, too, is that, while the causes of the inflation disease are bewildering and multifaceted (hence the need for a "comprehensive package"), they all boil down to sin—to excessive greed and hedonism on the part of some or all of the American public. Businessmen cause inflation by charging higher prices, unions by asking for higher wages, consumers by presuming to buy goods or borrow with their own money on credit, citizens by urging the poor old government to spend more. Since repeated exhortations from the White House to reduce our greed and enjoyment have failed, the time has come for the pain-master to get his jollies once again.

The Carter crackdown is on us, the consumers—strongly implying, of course, that our hedonism is responsible for inflation. Credit cards—that marvelous convenience of capitalism that enables us to enjoy first and pay later—have, like installment credit since the 1920s, long been the bane of Christian moralists. Now they are to be curbed and made more costly. Foreign oil is to be restricted once again, on the rather odd reasoning that inflation will be combated because the higher price will restrict consumption. On that reasoning, of course, we should hope for ever higher prices, unto the very stratosphere, as a method of "curbing inflation." Money market mutual funds, which, like credit cards, have nothing to do with generating inflation but are marvelous ways for ordinary people to try to catch up with inflation and not get wiped out, are also to be cracked down on and made far more costly. It is almost as if Carter looked around and discovered two dramatic recent innovations by which the lives of ordinary consumers and investors have been made more tolerable—credit cards and money market mutuals—and determined to punish us grievously for these sins.

Other forms of consumer credit will also be harassed, although of course not housing, which remains sacrosanct. And while Carter abstained from imposing wage-price controls, he did triple the staff engaged in monitoring the wage-price "guidelines" that have become a laughingstock but have probably helped to keep wage rates behind inflation and thereby ensure more pain for the nation's wage earners. Tax cuts were of course spurned as being "inflationary." To the contrary, pain will be imposed by subjecting interest and dividend income to the barbaric system of withholding taxes, originally imposed on wages and salaries as a strictly wartime and emergency measure during World War II.

In addition to consumer credit, other forms of *non*inflationary bank credit have been cracked down on in the new Carter program. They include certificates of deposit, which is a way by which banks can borrow from the public and relend without creating more money. Commodity speculators, especially in precious metals, have annoyed Carter by being able to keep ahead of the inflation, and so their borrowing has been made more difficult. Other proposals in the package were a gasoline tax that would drive up gas prices and a renewed appeal to Congress to hurry through the "windfall profits" tax on crude oil (actually an escalating excise tax on domestic crude), which will penalize domestic crude production and make sure that oil supplies will be smaller and prices higher. *This* is an anti-inflation program?

Of course, the federal government, too, is prepared to "sacrifice." In the cause of combating inflation, it is willing to reduce its budget by all of $17 billion, a whopping 2.8 percent cut. But before we throw our hats in the air, we must realize that this magnanimous cut is not made from the current 1980 budget but from the *projected* larger budget for the fiscal year 1981. This heroic belt-tightening by our masters means that the federal government will "only" *increase* its budget from 1980 to 1981 by 7 percent instead of the originally projected 9.3 percent. Now, *there* is "sacrifice" indeed!

The point in all this is that *there is no dragon* that the federal government must go out and slay, if only it had the will. Inflation is not caused by hedonism or greed out there in the economy; it is not the result of sinful actions by businessmen, unions, speculators, or consumers. It is not mysterious, nor is it especially multifaceted. A *price* is the result of interaction between money and the supply of a good; if a loaf of bread costs 70 cents, this is the result of interaction between the supply of bread and the number of dollars seeking to buy bread. The more money bidding for commodities, the higher their prices will be. Massive, chronic, and accelerating inflation can only come about because the supply of money has been increasing at a rapid rate. And this can only happen when the sole legal creator of new money—the federal government—expands its activities as the only legalized counterfeiter in the society and keeps increasing the money supply.

There is only one institution in America that is legally empowered to create new money—the Federal Reserve System—and it can keep increasing new dollars at will.

The Fed performs its counterfeiting activities by buying US government securities. By the arcane processes of the modern banking system, for every $1 billion of US government bonds purchased by the Fed, $6 billion of new money—of new checking deposits—gets created by the American banks. *This* is the process that has been generating inflation for decades. Week in and week out, the Fed enters the bond market, buys government bonds, and adds to the money supply by six times that amount.

In short, the federal government itself, through its Federal Reserve banks, is the one and only culprit in generating inflation. Last October Paul Volcker, head of the Fed, pledged to restrict the growth of the money supply through Fed operations. But since then, Fed purchases of assets, and consequently the money supply, have bubbled along merrily at the same inflationary rate. There is nothing in the new Carter package that addresses this key problem.

There is only one thing that the Fed need do to stop inflation: stop buying assets, period. The only institution that need sacrifice, that need suffer pain, is the federal government itself. If the government stops creating new money—that is, stops *inflating*—then inflation will at long last come to an end. But to do that, the federal government will have to stop scapegoating the rest of us and look to its own deeds. The only dragon that the white knight need slay is the white knight himself.

Murray Rothbard is a professor of economics at Brooklyn Polytechnic Institute of New York and the author of numerous articles and books on economics, history, and the libertarian movement.

money

The Silver Trading Caper

By Steve Beckner

WASHINGTON. Although silver trading has been resumed in New York, questions about what motivated its suspension in late January continue. How those questions are answered could have long-term repercussions for all US markets and for the American dollar.

The questions that are being asked in Washington, in New York, and, with fervid interest, in such competitive financial centers as London are: Did the silver-buying activities of big-time speculators like Nelson Bunker Hunt and family force the New York Commodity Exchange (Comex) to issue a "trading-for-liquidation-only" rule on January 21 in order to prevent "manipulation" of the market? Or, did other influential traders and companies with an interest in cheaper silver engage in manipulation of their own to drive the price of the white metal down?

The official justification for the suspension of all new position taking in silver futures contracts was that certain large silver speculators were threatening to create a "squeeze" on the supply of silver available for delivery. Many insiders, however, including sources at the Commodity Futures Trading Commission (CFTC) and Comex, believe the exchange's board of governors may have been motivated more by a financial squeeze on prominent members who had bet against rising silver prices by "shorting" the market—that is, selling silver for future delivery.

The Comex action had the effect of braking silver's rise and in fact causing it to fall from $49.00 to $33.50 an ounce within a few days. This allowed "shorts" to extricate themselves from their sell positions at lower prices, as it also accomplished the stated purpose of relieving the apparent shortage of deliverable silver. Further, it eased financial pressures on metals dealers, who had been getting huge margin calls on short hedge positions, which their banks became increasingly unwilling to finance. Gold traders with similar exposures may have benefited from a spillover effect.

A group of unidentified "longs" (those who had bought futures in anticipation of higher prices) are still considering a suit against the Comex for possible "conflict of interest," according to their counsel, Phillip Bloom. "A large number of people on that Board are known to have been short hedgers or sell hedgers," Bloom commented. "Many of them are such that they had inventories of metals that were not deliverable or in a deliverable state, who had been hedging them in the futures market and financing the cost of that inventory at major banks. And as the price of the metal continued to rise, the banks did not allow them to continue to borrow money for the purpose of paying variation margins [additional earnest money required to maintain a futures position]....So that may have precipitated the 'emergency'—not a squeeze."

Bloom has demanded all communications between the CFTC and Comex, as well as the proceedings of Comex meetings, the names of participants, and their positions in the market. The Chicago attorney, who says the Hunts are not among his clients, has not received a response to his Freedom of Information Request with the CFTC, and Comex has refused to release any information. Bloom vows that if Comex does not cooperate with his investigation he may "institute litigation and seek discovery." If he then determines there was "impropriety," his clients may sue for damages.

While this issue is being resolved, doubts about the integrity of American markets are rife. As a result, according to a number of traders and market analysts, US exchanges are losing business to foreign markets, and not only in silver. By reducing the liquidity of the futures markets, this drain of trading interest into foreign markets makes it more difficult for American producers and users of commodities to hedge their price risks via futures contracts.

Further, as prominent New York trader James Sinclair has noted, "if the interests who held those long positions in silver were bona fide international interests, specifically representing friendly OPEC nations, and we...reneged on their ability to take delivery, then we may have inadvertently seized their assets." That, he added, not only "takes interest away from our exchanges" but is "terribly negative for the dollar."

Sinclair says the "delivery squeeze," to the extent there was one, could have been handled through "negotiation" rather than through the drastic steps that were taken. "Longs" would have "acquiesced to taking reduced deliveries over deferred months." Bloom concurs, asserting, "My clients were willing to roll forward [their long positions]....Nobody asked them."

One Comex member, who did not wish to be named, has suggested that firms and traders with exposed "spread" positions had their "problems solved by the breakup of the silver market." (A spread, also called arbitrage, involves the simultaneous buying and selling of commodities in different months.) "You're either borrowing money on the physical and shorting the forward, or you're short the near [month contract] and long the far," he explained. Either way, the short side of the spread was creating painful financial pressures not offset by the long positions.

He said his firm had gotten a $90 million margin call on the short side of one of its spreads. "We're a moderate size arbitrageur," he noted. "If we're getting $90 million margin calls, my colleagues are getting $200 million, $400 million, and $800 million margin calls." Sooner or later, the banks "are going to shut you off," he declared. "And unless something

(Continued on p. 68.)

spotlight

Regulatory Reformer

By Robert Poole, Jr.

When they picked on Joseph Sugarman, the bureaucrats at the Federal Trade Commission had no idea what they were getting into. The typical mail-order company, charged with violating FTC rules, would have paid the demanded $100,000 fine and signed the FTC's consent decree—and risked damaging its reputation when the agency issued its triumphal press release. But most would figure it was less hassle than a long, costly legal battle.

Not Joe Sugarman. Outraged at what he considers "extortion" and denial of due process by the FTC, Sugarman counterattacked. He bought ad space in the *Wall Street Journal* and the *Washington Post* for a hard-hitting ad headlined "FTC REVOLT." Encouraged by the initial response, he went on to run the ad in 40 other newspapers and magazines—the major media in which his electronic products mail-order firm, JS&A, advertises.

JS&A came to the FTC's attention during January 1979. The Chicago area was reeling under 75 inches of snow, and most of Sugarman's employees couldn't get to work. On top of that, his computer system was on the blink, causing quite a number of orders to be "lost" temporarily. As a result, the company failed to ship many customers their merchandise within 30 days and failed to notify them of the delay (since it couldn't find their records)—both violations of the FTC's 1976 mail-order rule. The delays led some customers to complain to the FTC—and that led to a visit by an investigator.

Although JS&A solved its computer problem and filled all the orders, that didn't matter to the FTC. It had still violated the mail-order rule, and the agency wanted a $100,000 fine. If JS&A refused to cooperate, Sugarman was told, the FTC could subpoena all its records. He offered a compromise settlement under which JS&A would pay any damages to *consumers* up to $90,000, but the FTC refused to budge. Back came a subpoena for 600,000 company documents, which Sugarman says would have taken a year and a half to produce. At that point Sugarman dug in his heels. If the FTC can use the media to argue its case, he figured, why couldn't he?

Who is Joe Sugarman, and how did he get where he is? As an electrical engineering major at the University of Miami, he first discovered he had advertising talent when the owner of a barbeque restaurant challenged him to think of a way to increase his business among college students. But both coursework and copywriting were cut short when Sugarman was drafted in his senior year. Seeking something challenging, he volunteered for Army Intelligence training and wound up in Germany helping the CIA debrief Soviet defectors.

His tour of duty over, Sugarman and several partners started a ski-lift business, but he found he much preferred writing ads. He set up and ran his own Chicago-area ad agency for several years, until in 1971 he read a *Business Week* article on the birth of the pocket calculator. Convinced that the idea was a winner—but unable to persuade his major mail-order client to market it—Sugarman decided to

Joseph Sugarman

do it himself. Setting up shop in his Northbrook, Illinois, basement with $12,000 raised from friends, he rented 10 mailing lists for test mailings—and lost half the money. But two of the lists worked, making possible a successful follow-up mailing.

Since then, Sugarman's JS&A Group, Inc. has introduced dozens of new electronic gadgets—the flip phone, a pocket CB radio, a micro TV, an ion generator, and a sports radar, to name a few. Sugarman writes every ad and even sets the type and creates the layout himself. The ads "break every rule in the book" by featuring lots of words, by appealing to the reader's intelligence rather than his emotions, and by failing to include a response coupon (there's just an address and a toll-free number). But they *work!* JS&A sales have reached $12 million a year.

But the firm's growth now seems to be taking second place to Sugarman's anti-regulation campaign. In response to his ads, he's been deluged with letters, partly from well-wishers but mostly from others in business who have also been harassed by government agencies. "I've become something of a focal point for people to complain to," he explains, flipping through two four-inch thick piles of letters.

What does he hope to accomplish? Sugarman wants to solve not just JS&A's problem but the general problem of capricious bureaucratic regulation. Regarding the FTC specifically, he'd like Congress to repeal the 1976 Magnuson-Moss Act, which empowered the agency to write industry-wide regulations, rather than simply going after particular firms that engage in fraudulent or deceptive practices. It was one such regulation—the mail-order rule—that tripped up JS&A. He'd also like to see some procedural reforms, such as limits on the FTC's subpoena power and requiring the agency to pay the legal fees of firms that it sues unsuccessfully. (These latter reforms passed the Senate this winter.)

Longer range, Sugarman would like industry to adopt procedures that would eliminate the FTC's rationale for existence. He's proposed that the Direct Mail Marketing Association, for example, set up a voluntary certification program to designate ethical firms, with an easily recognized symbol to be placed in their ads (like the UL seal on electrical appliances). The certifying organization would carry insurance to reimburse any customers left hanging if a member firm went bankrupt.

This type of creative, free-market thinking is typical of a man who has practiced libertarianism all his life but never heard the term until libertarians started replying to his "FTC REVOLT" ad. "I would say my political orientation is definitely libertarian," he explains, having read one of the six copies of Robert Ringer's book that people have sent him. Others have enclosed pages from Ayn Rand's novels—which he plans to read as soon as he can find the time.

Joe Sugarman won big in mail-order electronics. And now this marketing genius wants to "win the battle of changing things" in the regulatory arena. After all, the tax revolt has its Howard Jarvis. Perhaps with a Joe Sugarman to rally its troops, the regulation revolt will be equally successful.

Bob Poole is REASON's editor. He is currently working on a story on the FTC for Reader's Digest.

arts & letters

movies

- **American Gigolo**
- **Cruising**
- **Chapter Two**
- **Being There**

Reviewed by John Hospers

• With the growth of explicitness in films, as one theme after another is exploited to its limits, another is dug up for presentation on the screen. It was probably inevitable that after horror had been carried to its ultimate in grisliness, sex would soon be in line for similar treatment. Two current films deal with previously "forbidden" aspects of sex life in America: **AMERICAN GIGOLO**, with a man who prostitutes himself to wealthy women in plush mansions of Beverly Hills; and **CRUISING**, with one aspect (sado-masochism) of the homosexual subculture in the seamier haunts of New York City. Both films end up being murder mysteries, and as mysteries both of them have such gaping holes or incongruities in the plot that they cannot rely on suspense alone, and thus both fall back on sexual explicitness for their effect, relying on the voyeuristic tendencies of viewers to witness visually what was previously off-limits to general audiences.

American Gigolo is set in Beverly Hills and Palm Springs and shows us a collection of hotels and mansions, parks and gardens, all exhibiting almost unbelievable affluence. The film proceeds at a leisurely pace, tracing the relations of the hero(?), Richard Gere, with a series of wealthy women. The plot begins to jell when one of them is murdered and he is framed as the culprit. Will the wealthy wife reveal that she was with him that night, thereby giving him an alibi, and losing the financial support of her politically prominent husband? Or will she keep still for her own protection? The angle is interesting, but one does not identify strongly enough with any of the characters to be vitally concerned with what happens to them. Some members of the audience may even feel (what the filmmakers certainly did not intend) that though the protagonist is innocent of murder he is justly framed anyway for other things he did that should be as strongly condemned as murder itself.

William Friedkin's (of *Exorcist* fame) *Cruising* is pitched at a much higher level of intensity, or at least movement, and has much more shock value. We are shown in considerable detail where the S&M crowds meet, and even some of the things that go on in their bedrooms. (It's rated R, but is almost an X.) One emphathizes somewhat more with Al Pacino in the role of undercover police officer, because of the extremity of his predicament, and yet one wonders, How could so "straight" a person be assigned as a decoy to attract the killer when he would be unable to go through with the required acts in the bedroom? Why should anyone in his right mind take on such a job under the conditions assigned—for example, no weapons? How could he be expected to defend himself against the murderer's knife when he is tied hand and foot? An interesting transformation occurs in him when he gets into the life of the characters he meets, but this development, though psychologically plausible in some instances, is not very plausibly presented to the film audience. (Friedkin, a skillful director, shouldn't have written the script.) The nudity, blood, and gore are so copiously served the audience that one cannot resist the conclusion that it was put there to titillate the audience rather than as essential ingredients in the story.

Nevertheless, the loud demonstrations against the film for being antihomosexual are without warrant. The film's wrath is reserved for a killer: that he happens to be of a minority sexual persuasion is not presented as a reason for moral indignation in the film. Anyway, *someone* has to be the villain. Some years ago the American showing of *Oliver Twist* was delayed for two years because the villain, Fagin, was a Jew. (This was Charles Dickens's idea, not director David Lean's.) But many villains in previous movies had been Irish or German or Japanese or English or even (heaven forbid!) red-blooded Americans; why can't a person of Jewish descent also be a villain once in a while? In the present film, the villain is a homosexual sadist, and there would appear to be no good reason why such a person should not also have his turn at villainy. In this one he does, with a vengeance that may excite some viewers and utterly repel others.

• Neil Simon is Neil Simon. If you liked the earlier plays/films, you'll probably like the new one. The gags are different, but the prevailing ambience is the same. So is the setting—New York—not Plaza Suite this time but plush New York apartments. The lines are cute and crisp, a few are memorable; all are more adapted to the stage than to the cinema. There is the offhand humor, the frothy lines occasionally touching deeper chords of feeling but never allowing itself to get too deep or take itself too seriously. There is brusque wit, a bit of cynicism, a touch of pathos, a tinge of nastiness here and there. But the real subject is romance—won, lost, anticipated, remembered. All very literate, very chic. But when a writer's main character is a writer (James Caan) and the heroine a stage actress (Marsha Mason), it's sort of like movies about making movies—the thing gets a bit inbred, and perhaps the author is scrounging around the bottom of the barrel for ideas.

It isn't quite true that if you've seen one Neil Simon play you've seen them all. Still, if you've gone through Chapter One you will find it continued without much change in **CHAPTER TWO.**

• In a *New Yorker* cartoon that has been taped to my office door for several years, a father is changing a tire in a driving rain and shouting to his children who are huddled inside the car, "No, we *can't* change channels! This is reality! This is the way it is!"

It is fortunate that Jerzy Kozinski wrote the film script himself, so as not to violate the intent of his ingenious and imaginative novel **BEING THERE**. The story line hasn't been changed, and some cinematic touches have been added that would have been ineffectual or impossible in literary description. The result is a highly unusual film, totally absorbing, hilariously funny, yet with a serious underlying theme that sustains it throughout.

Certainly the central idea is farfetched—that a simple gardener who has never been outside the mansion and grounds and whose entire concept of reality is based on what he has seen on television should, through a freakish succession of chances, become acquainted with America's foremost millionaire, have his every simple word taken for cryptic wisdom, be thought to have hidden depths in everything he says whereas in fact his every utterance is literal with nothing at all behind it, and by this means be catapulted to the presidency of the United States. But it is all done with such delightful tongue-in-cheek that we are quite carried away with this far-out conceit. Peter Sellers, acting the part of an inane and empty nobody, has delivered to us his most hilarious film within memory, and Shirley MacLaine and Melvyn Douglas perform their roles with

impeccable aplomb. This is one of the most original films in years, and not to be missed.

John Hospers is a professor of philosophy at the University of Southern California. His special interest is the area of aesthetics.

books

For Those Hard Investment Choices

The Hard Money Book.
By Steven K. Beckner.
New York: The Capitalist Reporter Press. 1979. 148 pp. $19 (paper).

Reviewed by John Pugsley

If the 1950s and 1960s were decades of the glorification of the benefits of common stocks, certainly the 1970s will go down as the decade that sanctified hard money investments. Accelerating inflation and monetary crises destroyed investor confidence in stocks and bonds, shifting interest to commodities and especially to precious metals. Initially, investors had narrow choices of types of investments and sources of purchase. Gold and silver were offered by a few coin dealers, or through foreign banks, and both the investments and the sources were unfamiliar to Americans. With the devaluation and subsequent decline in the value of the American dollar, however, the demand swelled for any investments that could preserve or even increase purchasing power in the age of floating exchange rates and blistering inflation.

Coupled with the demand for new investment vehicles and strategies that could cope with the economic changes, came a new trend in investment books. Ushered in by Harry Browne's prophetic work, *How to Profit from the Coming Devaluation*, the past 10 years have seen the number of books on gold, silver, and other hard money hedges grow to a veritable deluge. Most of them are written by investment advisors and are heavily laced with the personalities and pet investment ideas of their authors. As such, they provide the opinions of their authors but frequently fail to offer an objective review of hard money investment opportunities as a whole. For those investors who are less interested in special points of view on this field, and more interested in an overview of hard money investments and strategies, Steven K. Beckner, a reporter, has recently written *The Hard Money Book.*

Beckner puts his talents as a reporter to work to survey and categorize the entire spectrum of hard money investments. He discusses the track record and outlook for gold, silver, diamonds, and foreign currencies in a dispassionate and objective style. The reader will find this a good summary of the supply and demand factors affecting these assets, as well as a reasonably thorough look at the ways to buy and hold these investments. Beckner has traveled widely and interviewed hundreds of producers, consumers, investors, and the most prominent hard money investment advisors. In journalistic style, he avoids injecting his own personality into the work and steers the reader to conclusions by adroit selection of quotes and opinions from other sources.

In most cases the opinions Beckner selects offer a positive view of the future of hard money assets, but in a couple of cases he has chosen to concentrate on the opinions of individuals whose self-interest might get in the way of an objective evaluation of the merits of the assets. His discussion of the prospects for silver, for example, lean heavily on conversations with

Financial reporter Steve Beckner

Walter L. Frankland, Jr., executive vice-president of the Washington-based Silver Users Association.

Silver users—such as those companies in the photographic film industry, electronics, and the silver plating industry—are hurt by higher silver prices. Since silver prices are strongly affected by investor and speculator demand, bullish sentiments on future silver prices will tend to be self-fulfilling prophecies. It is not surprising, therefore, that Frankland levels a barrelful of pessimism against increasing silver prices. Unfortunately for Frankland, though, history has already demolished his arguments. When Beckner interviewed him in 1978, he asked Frankland to project silver prices for 1979. Frankland said he saw "no reason for it to be any higher, mainly because it is too high now." At the time of his statement, according to Beckner, spot silver was selling for $5.72 per ounce. Since that time the wildest forecasts of the silver bulls have been swept away.

Beckner offers some brief but interesting commentary on the various foreign currencies that are traded on the exchanges. He discusses the fundamental pressures that bear on the future values of each currency, as well as a variety of systems for taking advantage of price swings. Having spent several years as editor of *Deaknews*, the official newsletter of the Deak-Perera organization, Beckner is intimately familiar with foreign currencies. His concise but thorough discussion of the many ways they can be purchased and held is worth the price of the book. He also offers an understandable overview of bank notes, travelers checks, foreign bank accounts, foreign collections and payments, securities denominated in foreign currencies, as well as an explanation of the pros and cons of Swiss insurance, annuities, and endowments.

The final section of *The Hard Money Book* is devoted to a detailed discussion of the foreign currency futures market. This is a complicated subject, and while Beckner's treatment is clear and understandable, the section is biased toward the idea that, with the proper charting strategies, the solo investor has a reasonable chance of multiplying his stake. He discusses the conventional chart formations that technical analysts commonly use to predict price moves, such as downtrends, uptrends, congestion areas, tops, bottoms, double tops and double bottoms, wedges, head-and-shoulders formations, and ascending and descending triangles. Unfortunately, he fails to balance these discussions with the views of analysts who argue that charting cannot and does not work. The author's main source for the section comes from an interview with an individual whose self-interest conflicts with his objectivity: Dr. Wray A. Kunkle, vice-president at Paine, Webber, Jackson and Curtis in Washington, D.C. As an employee of an organization that depends on stock and commodity trading for its profits, it is not surprising that Kunkle suggests strategies and techniques that involve substantial trading and thus substantial commissions for the broker. As an observer who is extremely skeptical of technicians' claims that charting can beat the market, I am inclined to view Kunkle's arguments as a thinly veiled sales pitch designed to entice investors into trading in difficult if not treacherous markets.

In all, Beckner's book offers a broad look at the spectrum of hard money investment opportunities and presents a good cross-section of strategies for buying and trading in these assets. While it falls slightly short in areas where the author relies on opinions supplied by potentially biased experts, the majority of the book presents valuable material for any investor who is considering the fields of gold, silver, diamonds, and foreign currencies.

John Pugsley is the author of Common Sense Economics.

Is There a House In Your Future?

The Coming Real Estate Crash.
By John English and Gray Cardiff.
New Rochelle, N.Y.: Arlington House. 1979. 192 pp. $12.95.

Beating Inflation with Real Estate.
By Kenneth R. Harney.
New York: Random House. 1979. 288 pp. $10.

Reviewed by Bill Greene

The first question I ask when evaluating predictions of doom is, "What is the source?" Why? Because if a bond broker wrote a book on real estate, I'd expect him to praise bonds and knock real estate. Gray Cardiff and John English are bond brokers. They know nothing about real estate. They know very little about the bond market either—it turns out.

What do they have to say? Essentially, that during the frontier period of American history there were many boom towns that went bust. Many speculators in real estate lost their shirts. This is certainly true. But during the same period, astute real estate investors built up immense personal fortunes. The truth is that in any investment medium, amateurs and ill-informed persons who operate on the "greater fool" theory lose their shirts. Professionals who make deals with some degree of care and knowledge of the market will make a fortune. The "greater fool" theory, by the way, is simply that an investor says, "I don't know a thing about houses, empty lots, gold bullion, cocoa futures [or fill in the blank], but *everyone* is buying and thus some fool even more foolish than I am will certainly buy me out a higher price." Ben Franklin correctly stated that "a fool and his money are soon parted."

But Cardiff and English predict more than a few fools losing their money. They see a general and national real estate depression that will "not spare the homeowner." What is their remedy? Sell your houses, folks, and use borrowed money to buy long-term treasury bonds yielding 8¾ percent. Wow! The book was written in 1978 and widely distributed in the fall of 1979. By the time it hit the streets, if the authors had followed their own advice, they would have lost 100 percent of their savings. Long-term bond prices had their worst year in a decade, plummeting 30 percent as interest rates went up to all-time highs. Meanwhile, in 1979, house prices in northern California had their greatest single year's appreciation in history, rising about 30 percent.

The real estate speculator who did the opposite of what the authors advised and put 10 percent down on a property had a net appreciation of 300 percent. [Note: a 10 percent down payment on a property appreciating 30 percent gives the leveraged investor a 300 percent return on his money]. Thus the advice, when written, was just about as far from the mark as one could get. It was worse than bad advice; it was atrocious. A highly leveraged well-chosen single-family home or small rental property remains the best investment in times of double-digit inflation.

There is no hint of disaster in *Beating Inflation with Real Estate,* a 1979 release from Random House, by Kenneth R. Harney. Harney's book is not sensational. It contains no revelations. If it has any faults, they are the failings of the proverbial "good" man or woman—no sex appeal!

Beating Inflation is a good book—a basic primer on how to invest successfully in real property. Harney points out something that Cardiff and English ignore: most of the risk in real estate is assumed by lenders who provide up to 100 percent mortgages on which the astute investor is not personally liable. Uncle Sam, by giving huge tax deductions to real estate investors, helps out and provides investment capital in the form of tax refunds and subsidized loans.

But I get the impression the author acquired his knowledge by reading other books, not by first-hand experience. This is not to suggest that Harney plagiarized—he gives credit to his favorite real estate authors and practically admits that his book is an anthology of the ideas of others. He puts together many techniques used by intelligent real estate investors to make "no money down" deals and to reduce income taxes to zero. He emphasizes that from time to time certain areas are overbuilt. Also, *inexperienced* investors can be led like sheep to the slaughter by sellers of pie-in-the-sky real estate shelters or speculations. But he correctly indicates that real estate investments made *sanely* can be fun, can yield 200 percent per year returns, and can be engineered to be excellent tax shelters.

Harney tells us that controlling huge amounts of real property with virtually no investment and no risk—at the same time generating big "paper" losses for tax purposes—is the main appeal of real estate to investors. This point is entirely missed by Cardiff and English. They assume that 95 percent or better financing on many real estate deals today is like the financing of securities speculation just before the 1929 stock market crash. The difference between a 95 percent "margin loan" on stocks and a 95 percent loan on real estate is so obvious that it should require no explanation. But, since *both* books missed this basic point, you should get it here.

Stock market margin loans are always "call loans." If someone buys $100,000 worth of General Motors and manages to wangle a $95,000 margin loan (which is illegal today), and those stocks go down in value, the lender automatically issues a margin call. This means the investor must come up with immediate cash—or the lender will automatically sell the pledged stock. In the 1929 era, this meant that if hundreds of investors received margin calls on the same day, a wave of selling was automatically triggered until virtually all margined investors were wiped out.

Real estate loans are entirely different: If I borrow $99,000 to purchase a $100,000 duplex with a $1,000 cash down payment, the market value of real estate can go up or down, but it does not affect my loan. I will owe the lender about $1,000 per month (at 12 percent interest), and as long as I come up with my monthly payment, the loan can't be called. Generally, real estate loans are amortized over very long periods—like 25 or 30 years. As a result, in periods of tight credit, there are fewer real estate transactions but none of the violent price swings that happen regularly in the securities markets. For a stock to decline 90 percent in a *day* is not unusual. For real estate to decline in market value more than 20 percent in a *year* is almost unheard of—except in the face of unusual disasters like Three Mile Island or the collapse of the main industrial employer in a one company town.

Thus, while a credit crunch might cause a lull in the rising real estate prices we have been experiencing in the last decade, it will not create forced "panic selling" of single-family homes as predicted by Cardiff and English. This kind of selling sometimes happens in the stock market, but the vast majority of small property owners are what the stock brokers call "strong hands." Homeowners are unconcerned with "market prices" until they decide to move. The decision to sell a home is generally made as a result of a job transfer, birth, death, or divorce.

Securities are often bought by speculators who will dump the stock if the price doesn't rise in two weeks. Real estate owners work in a much longer time frame. They will hold investment properties around seven years in order to reap maximum tax benefits. Because of the tax laws, a sale in less than one year is seldom contemplated, and because of the 1031 exchange regulations, real estate investors or speculators seldom pull their funds out of real estate. Why should they, when they can invest the profits from one real estate deal into another without payment of taxes on the profits?

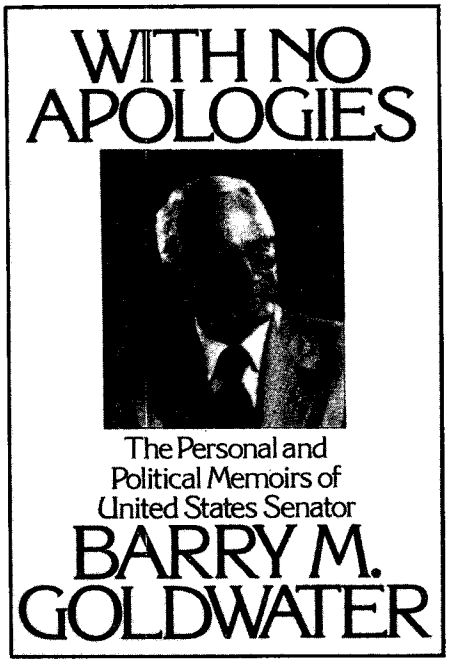
Harney recognizes all these facts and sees no evidence of a coming real estate crash. I agree with him.

Bill Greene is the author of Two Years for Freedom *and* Welcome to the Tax Revolt.

Goldwater Remembered

With No Apologies: The Personal and Political Memoirs of United States Senator Barry Goldwater.
New York: William Morrow. 1979. 320 pp. $12.95.

Reviewed by David F. Nolan



I must confess, I have a soft spot in my heart for Barry Goldwater. Like many libertarian activists, I first became involved in the political process via Goldwater's presidential campaign. And while I have never accepted his worldview or prescriptions in their entirety, I am convinced to this day that he was (and is) a man of integrity and intelligence, motivated by a fundamental—albeit imperfect—commitment to the preservation and furtherance of human liberty.

A reading of *Without Apologies* confirms this assessment and offers some intriguing insights into what makes Goldwater tick. Much of the book is devoted to accounts of personal experience—presented, for the most part, in chronological order—and there are numerous fascinating "snapshots" of the high and the mighty along the way.

We learn, for instance, that Barry liked Ike, looked forward to running against JFK in 1964, sympathized with LBJ's trials in office, and distrusted Nixon. His greatest contempt is reserved for Wayne Morse; *Without Apologies* contains several bitter references to Morse's defection from the GOP on the crucial vote to organize the US Senate in 1955. This defection cost the Republicans control of the Senate and, in Goldwater's opinion, kept the Eisenhower administration from changing things for the better.

For most libertarians, however, the personality assessments will likely be of less interest than Goldwater's expositions of his political philosophy and his stated concerns for the future of freedom. And there is no doubt that a devotion to individual liberty ranks high in the Senator's priorities. Throughout the book, the importance of freedom is stressed repeatedly.

In the very first chapter, he says: "To my mind there is a cause. That cause is freedom. We stand in danger of losing that freedom—not to a foreign tyrant, but to those well-intentioned but misguided elitist utopians who stubbornly refuse to profit from the errors of the past." This thought is echoed, a few pages later, by the statement that "the single essential element on which all new discoveries are dependent is *human freedom*" (emphasis Goldwater's).

He makes the observation—quite properly—that "the Constitution of the United States is one of the most radical documents ever offered to the world. It severely restricts the authority and power of he who governs and bestows a high degree of sovereignty on the governed."

In sum, Goldwater makes it abundantly clear that he recognizes the intrinsically adversary relationship that exists between individual rights and progress, on the one hand, and government on the other. And it is this element of his thinking that drew so many of us to his cause back in 1964.

But there is another side to Goldwater's philosophy, as well. It is rooted in the belief that "man . . . is still sinful, greedy, ambitious, lustful, self-centered, unrepentant, and requiring of restraint," with the concomitant view that we must be "governed by laws having their origin in divine justice." And, like most conservatives, Goldwater is never quite able to resolve the conflict between these two elements of his beliefs.

When translated into political doctrine, Goldwater's philosophy emerges as a contention that government is "necessary to protect the people from our enemies overseas, to restrain the greedy and lawless, and to provide a civil framework for the growth of commerce and industry." Everything else, he maintains, "could be better done by the people themselves without government interference."

As a libertarian, I find little there to quarrel with, on paper. But, alas, when Goldwater and his fellow conservatives apply this formulation to the real world, the tune changes—sometimes drastically. When push comes to shove, Goldwater's greatest concern (as revealed throughout this book and elsewhere) is with national defense. There is nothing wrong with this; indeed, if there is any charge that can fairly be made against some libertarians, it is that they are woefully *unconcerned* with defense—blissfully oblivious to the designs of the beasts in the Kremlin.

Conservatives do not make that mistake. But they are often all too willing to abridge our freedoms in the name of defending them. Thus, we find the Senator deploring the "emasculation" of the FBI and CIA and lauding the imperious, bigoted J. Edgar Hoover as a "national hero."

More examples of this split-level thinking: Goldwater bemoans the growth of government power, yet calls the Freedom of Information Act an "abomination" and the War Powers Limitation Act "an ill-conceived piece of crippling legislation." And, of course, it is the presence of these and other such internal contradictions in conservative thought which led to a parting of the ways between conservatives and libertarians a decade ago.

Still, for all his inconsistencies, it is hard not to like the Goldwater that emerges from the pages of these memoirs. Say whatever else you will, he is a man who has fought for liberty (as he conceives it) to the best of his abilities, for more years than most of us can remember.

And I still think he would have made a damn fine president.

David F. Nolan is employed in the advertising field. In 1971, after a history of leadership in conservative organizations, he set up the Committee to Organize a Libertarian Party.

It Could Have Happened Here

The Probability Broach.
By L. Neil Smith.
New York: Ballantine Books, Del Rey. 1980. 273 pp. $1.95 (paper).

Reviewed by Sara Baase

Many science fiction writers have presented pictures of libertarian societies, but in general they have been placed at some distant time in the future or on a distant planet or moon. Often we are told how and why they developed. Neil Smith's libertarian society is located right here, right now. He shows us what our world might have been like if something had happened just a little bit differently in 1776. His gimmick is the Probability Broach, a hole between our universe and an alternate one whose history was the same as ours until that critical year. But then the Whiskey Rebellion was successful, George Washington was assassinated, and the Federalists' constitution was declared null and void. The Articles of Confederation were revised with stringent limits on government power, and government influence steadily declined.

Smith's hero, police lieutenant Edward W. Bear—"Win," to his friends—stum-

bles through the hole in 1987 while investigating a political murder. He leaves a society, *our* society, where tobacco is prohibited, special permission is required for air conditioning and for private cars, old people beg in the streets, and the Department of Energy can close any business it deems not important enough to use "our nation's precious and dwindling energy reserves." Win finds himself amongst vigorously independent people and exciting advanced technology in a thriving anarcho-capitalist "North American Confederacy." He doesn't have much time to figure out what caused the two worlds to diverge because some of the villains followed him through the hole and are trying to kill him.

This book is great fun reading. The good guys and gals include some delightful characters. The fiercely independent, outspoken, 136-year-old Lucy, who fought the czar and the Prussians, hates government and loves politics, is bound to be almost everyone's favorite. There are laugh-out-loud lines and much spirited dialogue. There's the pleasure of learning that just about every libertarian hero from Lysander Spooner to John Hospers has been elected president of the North American Confederacy. "None of the above" won a term, too. On the other hand, a fellow named Jimmy-Earl is a peanut vendor.

Smith has sprinkled enticing examples of how things might have been throughout the book. Many inventions and discoveries came sooner. Men and women landed on the moon in 1949. Sophisticated home computers are as common and as taken for granted as electricity. Chimpanzees and cetaceans participate in society and have rights. There are four phone companies, and they provide very polite service. As we would expect of anarcho-capitalism, justice is provided by private associations.

Some readers will criticize Smith for arming his people; virtually everyone over the age of eight carries a weapon—or two. I don't think his argument for the weapons is very strong, but I'd rather let the author develop *his* libertarian society, idiosyncrasies included, than demand one with so little personality that we all accept it as *the* correct version.

The book has its flaws. The characters sometimes behave in improbable ways. The villains, particularly, seem to pass up a few good chances to eliminate the heroes. I think Smith has overestimated both the degree of technological advance that would have taken place and the degree of economic equality that would have been achieved. I find the latter a more serious problem than the weapons (which, by the way, Smith describes in loving detail).

I never really feared for the good guys after Win passed through the hole. Smith's description of that anarcho-capitalist world conveys such a feeling of wholesomeness, innocence, and optimism that the reader feels confident that good will win over evil there. It's a tribute to Smith's writing that the whole mood of the book changed with Win's entrance in the alternate world. The first few chapters were *depressing*. It was hard to imagine a believable happy ending there. The lack of fear, though, wasn't a lack of suspense. There remained the issues of what the bad guys were up to and how they would be defeated. And the major mystery of the book—exactly what happened in 1776 that made events in the two worlds diverge—is not solved until the very end. The solution should please all libertarian readers.

Sara Baase is a professor of computer science at San Diego State University.

Book Hints

a selective mention of books received

Entrepreneurs and others interested in surviving the times ahead might want to consult Franz Serdahely and Murray Miller's *How to Win the Battle against Inflation with a Small Business* (Wilmington: Enterprise Publications, 1980, 158 pp., $14.95). It suggests inflation-proof business opportunities, where not to put your money, how to use the barter system profitably, and some unusual tax shelters.

REASON contributors are showing up in several publications these days. Jerome Tuccille's 1978 guide to investment, *The Optimist's Guide to Making Money in the 1980s*, is now out in paperback (New York: Morrow Quill Paperbacks, 1980, 203 pp., $4.95). Viewpoint columnist Alan Reynolds appears in a collection of lectures given at the 1979 Ludwig von Mises Lecture Series at Hillsdale College (to which von Mises willed his entire personal library). The booklet, *Champions of Freedom* (Hillsdale, Mich.: Hillsdale College, 1979, 96 pp., $1.50), also includes lectures by William Simon, Benjamin Rogge, Dan Quayle, and George Bush (yes, *the* George Bush). Editor Robert Poole's December 1977 editorial on the minimum wage has been reprinted in the course book accompanying a college-level text called *Economics: Private and Public Choice*, edited by James Gwartney and Richard Stroup (New York: Academic Press, 1980, 880 pp., $14.95). Like a growing number of economics texts, this one points out the shortcomings of government intervention as it actually operates. Reason Foundation advisor and Nobel prize winner F. A. Hayek is the subject of an American Enterprise Institute pamphlet, *A Conversation with Friedrich A. von Hayek: Science and Socialism*, (Washington, AEI, 1979, 21 pp., $1.25, paper), an edited transcript of his "thinking aloud" at an AEI discussion, with a questions and answer period included.

Other interesting pamphlets include the new series of monographs on industry and the State put out by the Center for Education and Research in Free Enterprise at Texas A&M University (College Station, Tex.; all pamphlets 50 cents): *The Economics of Industrial Democracy: An Analysis of Labor Participation in the Management of Business Firms*, by Eirik G. Furubotn (26 pp.); *International Price Stabilization and the Less Developed Countries: Lessons from History*, by John R. Hanson II (23 pp.); and *Distortions in Official Unemployment Statistics: Implications for Public Policy Making*, by Kenneth W. Clarkson and Roger E. Meiners (15 pp.). Then there is the Center for Libertarian Studies' Occasional Paper No. 9, *Medical Malpractice: The Case for Contract* (New York: CLS, 1979, 67 pp., $2.50), in which author Richard A. Epstein attacks the rigidity of present laws as a return to the society of status and advocates contract standards.

And lastly, some comic relief. An amusing commentary on our overorganized society features illustrations by REASON's Randall Hylkema. It's called *Haga's Law* and is put together by William James Haga and Nicholas Acocella (New York: William Morrow, 1980, 191 pp., $8.95). And the wry, dry cartoons of Alexis Gilliland are collected in *The Iron Law of Bureaucracy* (Mason, Mich.: Loompanics Unlimited, 1979, 51 pp., $4.95).

—C. D.

money

(*Continued from p. 62.*)

comes along to turn around these markets, unless you work out of your spread positions, you could be in awful trouble."

Chris Feierabend, a New York commodity consultant, said he is "sure" the financial squeeze "had something to do with" the Comex action. He said those with "bull spreads" (long actuals or near months and short far months) were particularly strained by their banks. Asked if traders with such exposure may have used their influence to get silver trading shut down, one leading Manhattan bank officer with the knowledge of bank financing of arbitrage simply stated, "I assume that that's what happened."

What was the role of the CFTC? One silver trader asserted that the commission

came under great pressure from big silver users and shorts, who succeeded in persuading the commodities watchdog that their interests coincided with the "public interest." As a result, he concluded, "the CFTC probably advised them to liquidate only, and by that time the Comex had so many wounded members that it was only too happy to oblige the CFTC."

One well-placed CFTC source confided that the commission discussed in advance the use of trading for liquidation only at a closed meeting in early January with representatives of Comex, as well as the Chicago Board of Trade and Mid-America Exchange. (Hunt came to the meeting uninvited and was refused entrance, the source said.) Asked if such a discussion had taken place, Commissioner Robert L. Martin replied, "I don't know if it was discussed. It was not raised by the commission, because I suppose that it is always a consideration.... We didn't pound on the table and tell them you've got to do this or you've got to do that." But Martin went on to say that the CFTC's main "concern was with the shorts in the market who were not going to be able to perform." Martin said he was prepared to grant an extension of the rule if the Comex requested it.

CFTC officials say the commission received considerable input from companies with an interest in lower silver prices. One recalled "three or four meetings" with the Silver Users Association. Another stated he had talked to "several" representatives of companies with an interest in lowering silver prices. In particular, he said a representative of GAF Corp. "was all upset that, through speculation only, the price was going up."

He added that Dr. Henry Jarecki, president of Mocotta Metals Corp., was "very vocal to the commission." He noted that this leading precious metals dealer "just had everything on the line with their banks.... I suspect they had something to say about it." Dr. Jarecki, a Comex board member, failed to return a reporter's calls, as did Comex president Lee Berendt. Silver Users vice-president Walter Frankland said that his input with the CFTC was "not anything more than we have always called for." He did say, however, that he had advocated "forced liquidation until speculators come under (contract) limits." Frankland added that Comex experienced only an "apparent shortage" based on the "formality of its delivery requirement."

The latter CFTC source felt the closing of the silver market (until February 13) was "basically done by Comex members who had large short accounts and not by public customers." He did not know to what extent the commission influenced the decision, or was influenced to approve the decision by short interests. But, recalling the earlier suspension of grain trading, he noted, "the major grain people flooded Washington," and it "became quite apparent that it was all because of their actions that the commission closed down wheat trading for two days. The CFTC came out and said, This is in the public interest. We have to let everybody digest the news, when in point of fact it was the grain companies that had this tremendous clout."

Steve Beckner is a free-lance financial writer, the editor of Deaknews, *and the author of* The Hard Money Book.

letters

(Continued from p. 16.)

until the case was resolved.

After two months I received the decision of the Royal Customs Board. My appeal had not been tried because "the goods have been reexported by the Royal Post Office." The board, however, said that all facts were in my favor, the magazines were free of import duties, but as the magazines were reexported, the board was not able to make a physical check on the contents of the printed matter sent from REASON magazine and thus was not able to make a legal decision. I found this ridiculous, and very much supporting my claim in the article, that we had too much bureaucracy.

I wrote to the solicitor general, not with a formal appeal, but to question whether the Royal Customs Board and the Royal Post Office had handled my appeal according to the rules. The solicitor general asked both agencies to give their views on the matter. The Royal Customs Board said they were sorry but that the Royal Post Office was to blame. The Royal Post Office, on the other hand, said that they were not to blame at all and that the only chance of a person receiving goods charged with incorrect fees was to pay the fees and make the appeal afterward. If the ruling was in his favor, which was very unlikely, he might get his money back.

The solicitor general found that the authorities had handled the matter according

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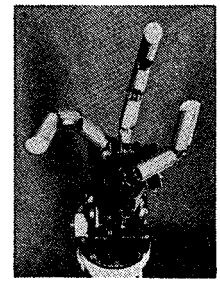

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to reasonable practice, although the Post Office could be criticized for a number of faults. With a promise that planned negotiations between the directors general of the Royal Customs Board and the Royal Post Office would very likely solve any future problems, the case was dismissed.

Carl G. Holm
Stockholm, Sweden

Money Matters

I would like to add a clarification to a point made in the April Trends about gold backing of the dollar. The "chief economist" of the French bank Societe Generale was quoted as saying that "today's high gold prices make...US gold reserves equal to half the US money supply." This depends on what one takes to be the US money supply. As of the end of October 1979, the gold price had to be about $400 for 100 percent backing of "currency in circulation;" about $1,430 to back *M*1 (currency + checking accounts); about $3,900 to back *M*4 (*M*1 + savings deposits + large CDs); and about $6,400 to back *M*5 (*M*4 + deposits at mutual savings banks + S&L and credit union shares). And if you add in $965 billion "Eurodollars," the figure comes to $10,035! Thus, it is obvious that this economist had in mind *M*1, which is the lowest measure used nowadays.

Comparing these figures with those at the end of 1928, just before the Great Depression, is startling.

Gold Price for 100% Backing

	1928	1979 (Oct.)
Currency	23.49	397.53
*M*1	186.52	1428.00
*M*4*	338.54	3884.00
*M*5* *	444.63	6395.00

* Same as *M*2 until 1961 (now *M*2 + large CDs)
* * Same as *M*3 until 1961 (now *M*3 + large CDs)
(All data based on *Banking and Monetary Statistics* (FRS, 1943), Milton Friedman and A. J. Schwartz, *Monetary Statistics of the United States* (1970), and various issues of *Federal Reserve Bulletin*).

The table also shows that *M*1 is a *misleading* indicator, since it has increased only about half as much since 1928 as the other measures (currency, *M*4, and *M*5). But this is only to be expected, as more and more people take their money out of non-interest bearing checking accounts and put it elsewhere. This point can also be seen from a comparison of 1921-28 and 1957-79 increases in the money supply (as measured against US gold reserves).

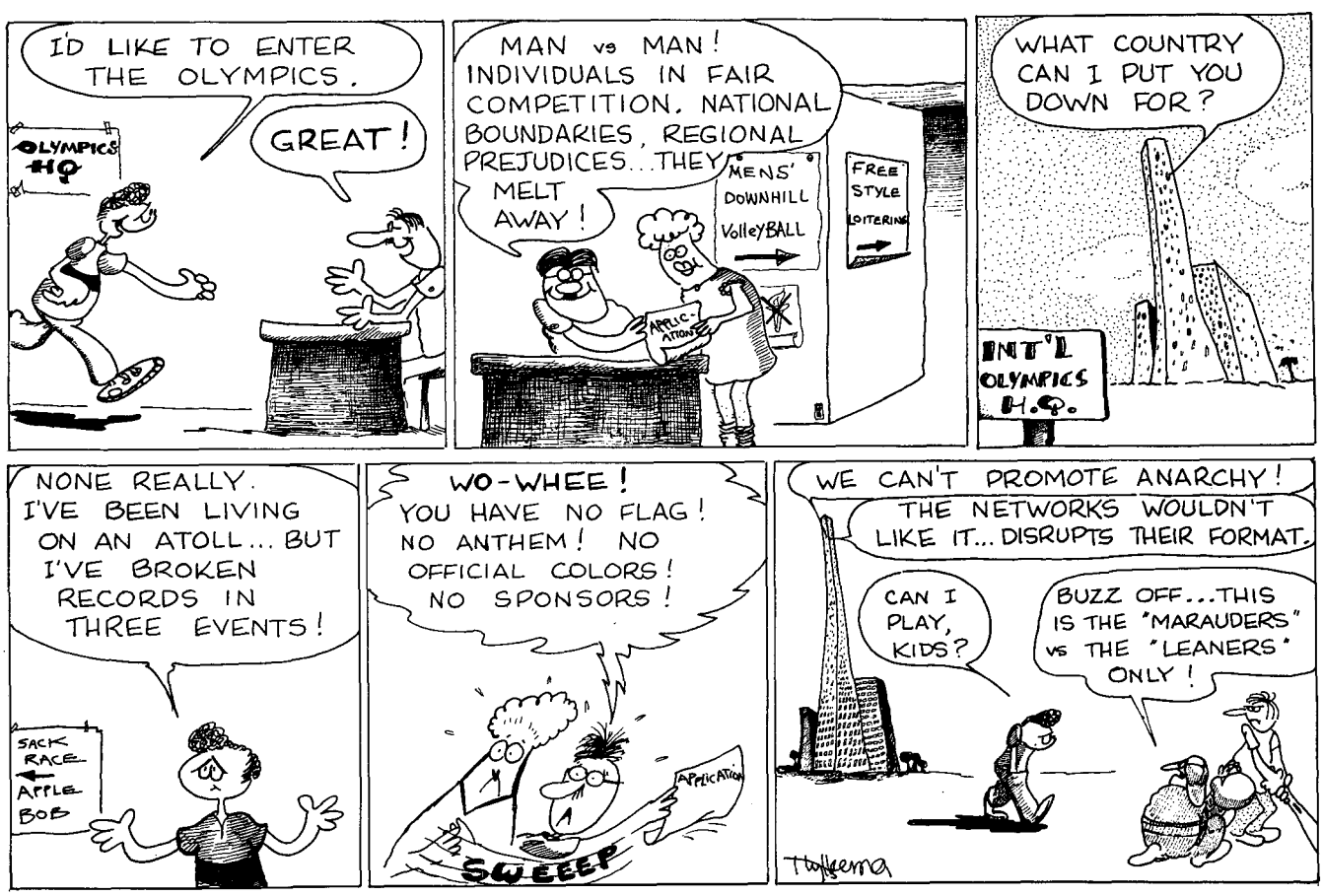
Money Supply Growth

	% Increase	% Inc./Yr.
1921-28		
Currency	- 8.5	- 1.3
*M*1	+37.6	+4.7
*M*4	+59.5	+6.9
*M*5	+69.6	+7.8
1957-79 (Oct.)		
Currency	+ 817.4	+10.7
*M*1	+ 586.2	+ 9.2
*M*4	+1212.2	+12.5
*M*5	+1451.5	+13.4

Bruce K. Bell
Santa Barbara, CA

rudebarbs

by Randall K. Hylkema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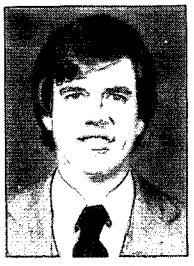

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As speechwriter and ghostwriter for 26 political candidates, Michael has written 109 articles and speeches. His provocative essays

in libertarian movement publications ("How to Get Converts Left and Right" in *Reason* and "The Late Great, Libertarian Macho Flash" in *Frontlines*) have stirred a storm of controversy and become underground best-sellers.

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ABORTION AND THE DRAFT: BOTH AGGRESSION. Doris Gordon's *Congressional Record* article: long SASE, LIBERTARIANS FOR LIFE, 13424 Hathaway Drive, Wheaton, MD 20906. (Other literature: $1.00)

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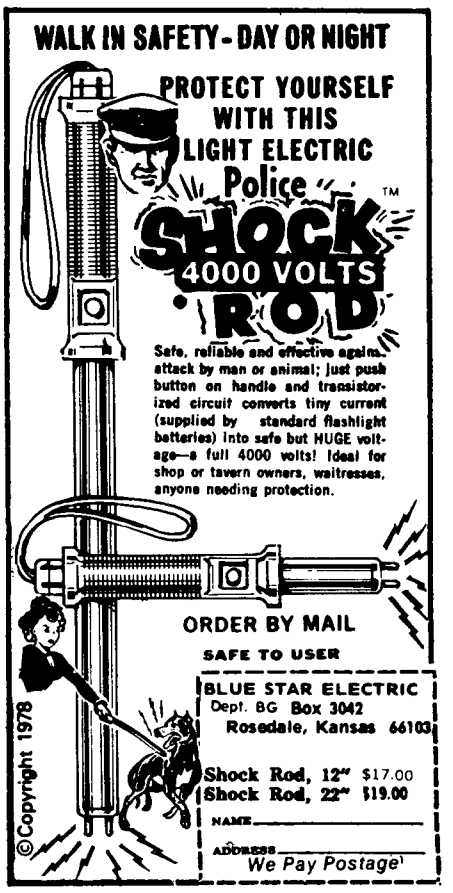
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Wage Your Own Personal Tax Revolt

Like the early pioneers who started this country, many people are rebelling against the near confiscatory taxation at all levels of government. The federal government consumes the taxpayer's cash at the rate of over $800,000 per minute, and the amount that is wasted is scandalous. The citizens are mad as hell and they're not going to take it any more.

There is but one answer left!

The U.S. was founded by a group of individuals who rebelled against the oppressive policies of King George in England. Today, this same spirit of independence, a uniquely American phenomenon, underlies a growing displeasure with government tax and spending policies. This viewpoint is a healthy sign. Our society can remain the freest and most prosperous in the world if government power is held in check by us, the citizens who make up the country. Recent passage of laws (such as Proposition 13) are an indication of a growing wave of protest against wasted tax dollars. The effort is getting stronger and more vehement every day.

The largest tax each one of us pays is Federal Income Tax. Yet, the largest corporations and the wealthiest individuals often pay the least amount of tax. According to an article in a leading newsletter, 17 huge corporations paid no federal income tax in a recent year, although they had a world-wide income of $2.5 billion. Numerous tax loopholes were used. The list includes United States Steel, Bethlehem Steel, Armco Steel, General Dynamics, Singer, Phelps Dodge, American Airlines, Philadelphia Electric and The Chase Manhatten Corporation. The burden caused by these non-taxpayers must be assumed by "somebody." "Somebody" is always the wage earner. There is, therefore, a major inequity under the law which favors the wealthy and, most especially, corporations. In America today we have what could be called a "Corporate Society."

Some individuals have become so upset with these startling inequities, they have stopped paying taxes and have in many cases even ceased to file tax returns. This approach, however, is frought with danger and has resulted in stiff fines or prison sentences when the government locates and prosecutes the courageous individuals.

You Can Become Part of "The Corporate Society"

Rather than break the law and suffer serious consequences, there is a safer and more viable alternative. You can use the same type of smart thinking as those who own and control great wealth. The big corporations are not necessarily immoral. However, they do get the best advice available on tax matters.

You, as an individual, can now use all the tax loopholes for your own self interest. Thus, you legally gain the advantages yourself as do the huge corporations. Rather than break the law, you can use it to your advantage. Perhaps the best way to accomplish this, as well as reduce your tax burden is through incorporation, the legal form of tax rebellion.

Surprisingly enough, the government encourages incorporation with a number of favorable laws, especially in the area of taxation. In fact, it is rare to find a successful individual who is not incorporated. Incorporation is favored by nearly all millionaires. It is one of the causes of wealth, not its effect. Think about it. Can you think of a single wealthy individual who doesn't own and control his own corporation? It is rare indeed. Let's face it, the first step toward achieving the American Dream in our corporate society is probably incorporation.

To add even more impetus to the idea of starting your own corporation, passage of the recent Revenue Act makes incorporation the ultimate tax shelter. This act and the earlier ones close the door to practically all other tax shelters and loopholes. The tax rate on corporations (especially smaller ones) has been substantially reduced, to as low as 17%.

Favorable laws such as the investment tax credit are most helpful when buying equipment. Even if you incur losses in one year you can deduct those losses over several profitable years.

More Advantages. . .

You can set up a corporate medical plan wherein you deduct from your taxes every dollar spent on medical and dental care, drugs, and health insurance for yourself and your family. You can also get tax deductible group life insurance even if the "group" consists of only one person.

It is important to note that potential tax savings are not the only reason to incorporate. Another chief value is that it limits your liability to the assets of the corporation in the event of a lawsuit. If you do business as an individual or partnership, you can be sued personally, which could put your house and other assets in jeopardy

You can put more money (25% and more of income) into your corporation pension plan. This is more than a traditional "Keogh" plan which has a maximum contribution of $7,500 a year, or even an I.R.A., where the maximum that can be sheltered under special circumstances is only $1,750.

In these times of growing inflation and periodic ups and downs of the economy, your own corporation is probably the only way that you may maintain control over your economic destiny. And you can often benefit from incorporation without leaving your present job. More about that in a moment.

You Can Incorporate Simply, Easily and Inexpensively.

Up until now, throughout the majority of history, incorporation had one major drawback: high legal fees. Lawyers today charge stiff fees, up to $2,500 for incorporation. The truth is that you can easily incorporate yourself for under $50. A remarkably easy and inexpensive method of incorporating is contained in a book called *How To Form Your Own Corporation Without A Lawyer For Under $50.* It comes complete with all the tear-out forms required to start your own corporation . . . minutes . . . bylaws . . . everything you will ever need. The author, Ted Nicholas, has helped thousands of people start their own corporations and has saved them millions of dollars in the process – and many millions more in taxes.

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To receive your copy of *How To Form Your Own Corporation Without A Lawyer For Under $50,* write your name and address on a piece of paper along with the words "Corporation Book & Bonus" and send it with your check or money order for $14.95 to Enterprise Publishing, Inc., 725 Market Street, Dept. RE-05C , Wilmington, Delaware 19801. Send for the system now. Let us help you wage your own personal tax revolt. Important note: The full price of the book is tax deductible. Act Now!

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"Over and over again courts have said that there is nothing sinister in so arranging one's affairs as to keep taxes as low as possible. Everybody does so, rich or poor; and all do right, for nobody owes any public duty to pay more than the law demands; taxes are enforced exactions, not voluntary contributions. To demand more in the name of morals is mere cant." **Judge Learned Hand**

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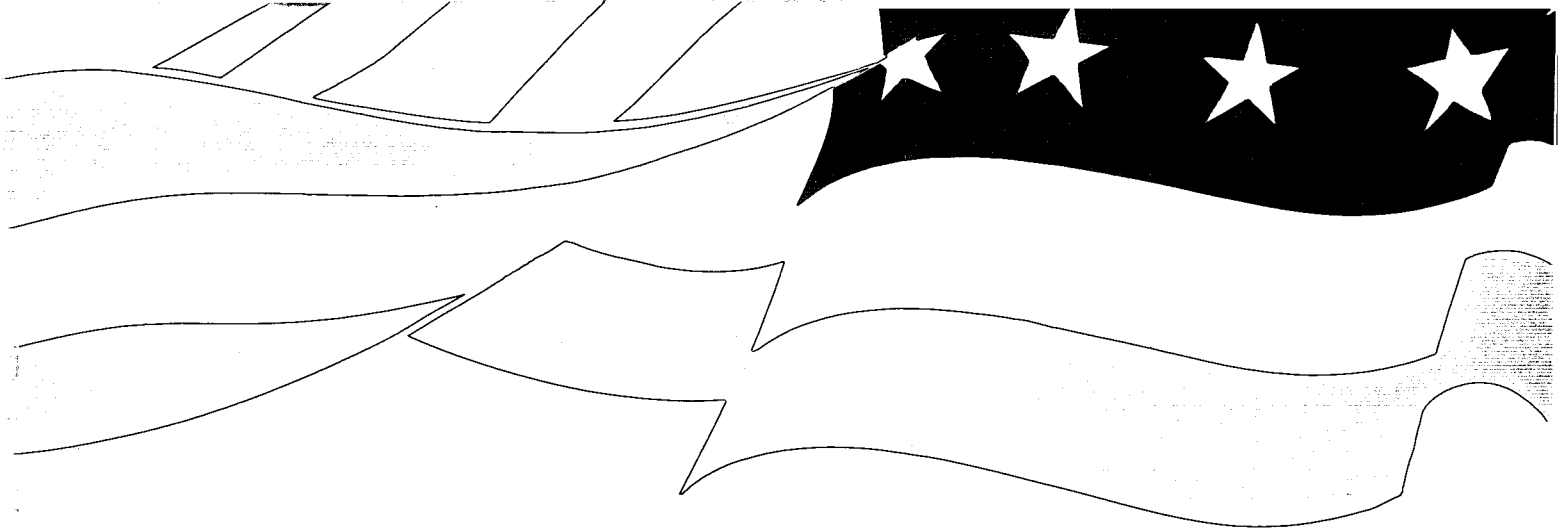

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The seminar format will consist of 2½ days of a) general session speaker presentations, b) informal workshops wherein speakers may expand upon their ideas, explain particular investment strategies, answer questions, etc., c) a closing panel discussion in which guest speakers will reply to the question, "During the '80's, what changes do you expect in the economy; how may investments be affected?" and d) social functions offering the opportunity to meet individuals with similar interests. (There will be a reception/ buffet on Saturday night and a banquet on Sunday night.)

The registration fee is $225 per person ($400 for one attendee and spouse) which includes all of the above functions. The number of attendees is strictly limited by the general session hall capacity. Reservations will be held only upon submitting the registration fee.*

Note: *For additional seminar information, please see the following page.*

Enclosed is my registration fee for the **INFLATION AND GOLD SEMINAR**, May 24, 25 & 26, 1980, at the Radisson Chicago Hotel.

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INFLATION AND GOLD SEMINAR

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RECESSION; what to expect
CORPORATE PLANNING; controls and taxation
OPEC and NUCLEAR ENERGY; what are the alternatives
CAPITALISM and the GOLD STANDARD; what is the connection
GOLD and SILVER; what causes price fluctuations
INVESTMENTS; strategies for preserving assets, capital growth and speculation

GUEST SPEAKERS. . .

None of the following speakers are connected with Tempor Corporation and their appearance as a guest speaker is not intended to imply an endorsement of its divisions or policies.

Petr Beckmann, professor of electrical engineering at the University of Colorado, is author of the book, **The Health Hazards of Not Going Nuclear**. This book clearly explains the nuclear controversy and, thereby, refutes the hysterical cries of the anti-nuclear crowd. Dr. Beckmann is publisher and editor of the pro-science, pro-technology, pro-free enterprise monthly newsletter, **Access to Energy**. This publication informs the layman on the technical background of new developments in all branches of energy, as well as the economic and political background of energy matters.

Robert M. Bleiberg as Editor of **Barron's National Business and Financial Weekly**, has discussed the consequences of government intervention in the economy for many years. The timely, accurate and important information contained in **Barron's**, assures it of wide readership in business and political circles. Mr. Bleiberg's warnings often go unheeded but the perpetrators of destruction may not plead ignorance.

Jan R. Goergen is Chairman and Chief Executive Officer of Intercap Corporation, a financial advisory and international money management firm which is responsible for overseeing the management of six billion dollars for an OPEC nation. He is knowledgeable on the OPEC view of the West. Mr. Goergen's clients include individuals as well as corporations and institutions; his advice on finance, investments, financial planning and tax reduction strategies is sought internationally.

Robert Hessen taught in the Graduate School of Business at Columbia University until 1974. Since then, Dr. Hessen, a historian, has been a research fellow at the Hoover Institute on War, Revolution and Peace. His most recent book, **In Defense of the Corporation**, explains the nature of the corporation and shows the valuable tool it provides a free society. Importantly, he offers a systematic rebuttal to yet antother of Ralph Nader's attempts to return us to a pre-industrialized society.

Douglas E. Johnston, 1938 graduate of Williams College and registered representative with the Dallas based securities firm Rausher, Pierce, Refsnes, Inc., has been specializing in gold and gold mining shares for the last fifteen years. He has written numerous articles on these investments and is a frequent speaker on the subject.

Michael Linden is Editor and Publisher of **Hard Facts**, a gold, silver and precious gems newsletter which examines the many unrecognized parallels between freedom and investing. An advocate of laissez-faire capitalism, Mr. Linden is an investment advisor, author and public speaker who recommends investment portfolios designed to protect assets from government plunder.

Lawrence T. Patterson, financial planning consultant, is editor of the world news/investment **Patterson Strategy Letter**. He is an energetic promoter of economic education who constantly directs attention to media censorship of international events, inaccurate financial reporting and government activities which threaten individual financial security. He is a knowledgeable speaker on international banking and investing.

Leonard Peikoff, Keynote Speaker, is a professor of philosophy. Although he is not acquainted with the field of investment counseling, he, in his profession, elucidates the basis upon which all decision-making follows. Dr. Peikoff is a long-time writer and lecturer on Ayn Rand's philosophy of Objectivism. His excellent lecture courses are taped and leased throughout the world; his most recent course deals with presenting ideas effectively. He is author of a forthcoming book, **The Ominous Parallels**, which discusses the similarities between pre-Hitler Germany and America today.

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John A. Pugsley, Editor and Publisher of the monthly periodical, **Common Sense Viewpoint**, is a businessman, investment advisor and author. His varied experiences and intensive study of the relationship between world economic events and investment values, led to writing his best-seller book, **Common Sense Economics.** His second book, just released, **The Alpha Strategy**, offers the first absolutely risk-free, inflation-proof and tax-free strategy ever developed for the middle class saver and investor.

Walter E. Reed is the author of **Commodities as an Independent Business Venture**, a course he teaches to a maximum of 12 persons a year. His thorough grasp of the economic factors that are responsible for commodity price activity, as well as the strategies of applying that information, has led to success as a professional commodities trader and has earned him an international reputation. Mr. Reed is an independent commodities consultant, and resides in San Jose, Costa Rica.

George Reisman is currently Associate Professor of Economics at Pepperdine University in Los Angeles. He received his doctorate from N.Y.U. where he studied under the late Ludwig von Mises. Dr. Reisman, an outspoken defender of capitalism, is the author of the recently published book, **The Government Against the Economy**, which explains how our government is wrecking our economic system through policies of inflation and price controls.

Irwin A. Schiff is author of **The Biggest Con . . . How the Government is Fleecing You**, the primer of many popularizers of the hard money movement. Carefully researched and documented, this book presents irrefutable evidence of the immoral, destructive nature of present U.S. federal government activities. Mr. Schiff is also well known for his aggressive tactic of bringing attention to these activities as a tax rebel.

John Van Eck is founder and President of International Investors, Inc. (III), the largest and oldest U.S. gold-oriented mutual fund. With an extensive background in securities and a grasp of the nature of an inflationary economy, Mr. Van Eck alerted investors early as to the potential of gold and silver mining shares. III now handles investments in precious metals mining and finance companies amounting to over $100 million.

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